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THE ECONOMIC, FINANCIAL
AND POLITICAL STATE OF
GERMANY SINCE THE WAR

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LECTURE I

GERMANY AT THE END OF THE WAR

It seems that neither an individual nor a people can learn anything of practical use from the experiences of others; that, on the contrary, one can learn wisdom only from one's own experiences and sufferings. Before turning to my subject, I venture to express the conviction that, in view of the sound common sense which characterizes your nation and of the wise political and economic leadership of your country, the American people will never find themselves in difficulties similar to those in which the German people have been involved.

At the same time I believe that the history of the breakdown and reconstruction of the German currency, and of the decline and recovery of German economic life, is interesting beyond that of most other chapters in the economic history of the civilized peoples of this world, and that, for this reason, it is well worth while to glance back at it for a moment.

Above the history of the breakdown of the German currency one might write a motto, which is, I consider, applicable to all peoples and to all times: when a people has made the fatal resolution to give no more than its little finger to the devil of inflation, this devil is not content merely to take the whole hand; he is not satisfied until he has devoured the whole nation, bones and all.

What was the currency situation in Germany at

the end of the War? When—after an heroic struggle which, I believe, will be regarded in the history of the world as a proof of extraordinarily strong national will and of self-discipline and patriotic sacrifice beyond comparison, as well as a test of a great and powerful gift for organization—in November, 1918, the German people finally collapsed, completely exhausted physically and mentally, we were already in the toils of inflation. The first measures undertaken by the German Government in the sphere of currency policy, after the outbreak of war, had, in August, 1914, opened the way to this inflation. In addition to the suspension of the obligation of the Reichsbank and private note-issuing banks to make specie payments, two measures must be particularly considered: first, the creation of loan offices which could issue paper money as an advance on paper securities and goods and which thus created a considerable amount of additional purchasing power; and second—and this was, in my opinion, the decisive step in the introduction of inflation—the empowering of the Reichsbank, which was practically a duty in view of the close relations between the Reichsbank as it then was and the German Government, to accept treasury bonds and bills as cover for paper currency. In this way the German Government was enabled to pay its debts with freshly printed paper money, the first dangerous step on the broad and easy path which leads to the limbo of inflation.

Owing to the highly patriotic temper of the whole German people and the patriotic spirit of sacrifice shown by all classes of the population, who simply flocked to place their savings at the disposal of their

country in its hour of need, the subscriptions to the first four 5 per cent War Loans were such a great success that, by the summer of 1916, not only was it possible to redeem the debt which the Government then owed to the Reichsbank, but in addition a surplus balance of about five billion marks remained. A change came over the scene after the summer of 1916. The power of the population to save was exhausted and the subscription to the War Loans, which was moreover to a large extent only apparent, as it had been artificially made possible by advances from the loan offices, fell short of the national floating debt. And so it came about that, up to the end of the War, the German Government had unfunded debts approaching forty billions of marks, which, in the first instance, were financed by the Reichsbank, that is to say, by the printing of paper money.

It was in Germany that this mistaken form of financing the War took its severest revenge, this form which Germany and moreover France and the majority of the belligerent countries on the continent had adopted, namely, the financing of the War, simply by the incurring of debts. This principle may be feasible and even defensible for a war of short duration. But for a struggle which was to last for years and to destroy innumerable values, the system contained in itself the germs of currency collapse.

Great Britain, as is well known, followed another course. As early as September, 1914, a wise and far-seeing government had doubled the income tax and again raised it appreciably in the years 1915 and 1916, as the War was still in progress.

Meanwhile, in Germany, as late as the autumn of 1915, the then Financial Secretary, Helfferich, who

later played an important part as a leader of the German National Party, was confident of an early and successful conclusion of the War and declined to finance expenses by increased taxation.

Although later on Germany also decided to increase existing taxes and introduce fresh ones, notably the War Profits Tax and the Turnover Tax, the only result was that a small fraction—about 5 per cent—of Germany's war costs was met from taxation, while England covered from one-fifth to one-quarter of her war expenses without borrowing.

This dangerous form of German war finance was just as sharply criticized by clear-sighted foreign observers as by German financial experts whose financial vision extended beyond the narrow boundaries of Germany. Among these latter, and there were many, I would like to mention Dernburg, who, in the late autumn of 1917, publicly criticized the Government for its course of action in the question of war finance in an unusually severe manner.

And so it came about that, at the conclusion of the War, Germany had a funded debt of over one hundred billion marks in 5 per cent War Loans and an unfunded debt of about forty billion marks. Since, as has already been stated, the unfunded debt was covered in the first instance by the printing press, the result was that this form of finance caused an extraordinary increase of currency, balanced only to a very small extent by the withdrawal from circulation of other legal tender—mainly gold coin and token money.

At the beginning of the War, Germany had a currency circulation of about six billion marks, of which about two billions were Reichsbank notes and the

rest mostly gold coin and token money. This circulation had not increased materially by the end of the first year of war, but it must be noted that the gold was gradually withdrawn from circulation and replaced by bank notes. Even at the end of the second war year, the circulation, which had increased to about ten billions, could still be called to some extent normal. The same may be said of 1916, with its thirteen billions, bearing in mind the fact that, owing to the occupation of foreign territory by the German army, an appreciable increase in the area in which the mark was in circulation had occurred.

From the beginning of the year 1917, the signs of inflation became more and more clearly apparent. At the end of the year 1917 the circulation was 19.5 billions, and, by the time of the armistice, it had risen to 28.4 billions or about five times the normal amount.

And thus we found ourselves in Germany, at the end of the War, in a precarious state of inflation. The fact that this inflation had not yet made itself evident with its full devastating effect is due to two causes. So far as the valuation of the mark in foreign countries enters into question, we must remember that Germany was, economically speaking, almost entirely cut off from the outside world, so that—no currency regulator whatever existing in the form of an exchange of commodities—the valuation of currency was a somewhat arbitrary matter. It was determined by the belief of the international public that Germany, in spite of her terrible defeat and of the acute symptoms of revolutionary fever which were wasting her strength, would yet recover and gradually bring her currency back to something ap-

proaching its normal exchange rate. The result of this belief was that nearly all neutrals who had bought marks during the War, held on to them at first, in spite of their losses, as experience seemed to have taught them that the currency of a great nation, which has lost a war, may indeed suffer from temporary depression owing to the influence of defeat, but will approach par once more when peace has been concluded. In this way the valuation of the mark abroad at the end of 1918 was strongly influenced by the belief in Germany's recovery, and only in this way can we explain the fact that, at the end of 1918, the mark was still quoted on the international market at the relatively high rate of twelve cents or about 50 per cent of its par value.

At the same time the internal purchasing power of the mark did not fully reveal the stage of inflation which had already been reached, since prices were deprived of their natural power of expansion by the compulsory economic regulations in Germany and the official maximum prices for many articles of daily use. In spite of this there was an unmistakable rise in prices, based on a foundation of inflation. Taken altogether, if the wholesale prices at the outbreak of war are put at one hundred, the commodity index had risen at the time of the armistice to two hundred and thirty and the wage index to about two hundred fifty.

And so, as early as 1918, the situation of Germany, seen from the angle of the currency, presented an extraordinarily dangerous appearance. But this was not the gloomiest point in the financial balance-sheet which no one in Germany had drawn up in its final terms, owing to the needs of everyday life and to the

lack of grasp with which this great new problem was treated; but now we can, and must, strike this balance in retrospect.

In the first place the wealth of the German people had decreased very much during the War. For years Germany had really been almost entirely cut off from the world's reserves of foodstuffs and raw materials by the blockade, so that she had imported very little. On the other hand, the German export trade had come almost to a standstill, not only owing to the artificial closure due to the blockade but also owing to the fact that all her then existing internal industrial strength had been devoted to the maintenance of the army. Germany was not even in a position to pay in exports for the comparatively unimportant purchases she was able to make abroad.

Germany's adverse balance of trade during the War reached at least fifteen billions; this balance had of course to be met by small payments in gold, by the sale of German-held foreign stocks and by foreign currency obtained on credit.

So far as gold is concerned, the population of Germany was almost entirely deprived of its gold during the War. As early as the beginning of the War it was considered a patriotic duty in Germany to exchange all gold coin for paper money at the public treasuries, and all the great organizations placed themselves at the disposal of the Government for this purpose, especially the press. I myself remember that, by means of an appeal in the *Leipziger Tageblatt*, of which I was at that time the publisher, I was able to collect nearly one million dollars' worth of gold coins and hand them over to the Reichsbank. With the increase in Germany's need, these contri-

butions in gold assumed even more beautiful and touching forms which recalled the days of the great German struggle for freedom in 1813, when the whole population sacrificed their valuable belongings to the country.

Once again, as a hundred years before, the old phrase on the little iron memorial medals handed over in exchange for gold, applied to every man and woman with patriotic feelings "Gold I gave for iron" or, in its new form, "Gold in defence I gave; iron 'tis my honor to have."

This voluntary handing over of gold—followed later by that of other precious metals and jewels—resulted, despite the export of specie to neutral countries, in the gradual rise of the gold reserve of the Reichsbank from 1.25 billion marks to its highest point of rather more than 2.5 billions.

The taking of gold from the German people had, it is true, caused no economic disadvantage—it may even be said to have had a favorable effect on our trade balance. In any case we gave up a possession which bore no interest. But the giving up of stocks and shares was a much more delicate matter. At first an endeavor was made to obtain the voluntary transfer to the State, as in the case of gold, of such securities in terms of foreign currency as were in the private possession of German nationals. When this system no longer yielded sufficient results, recourse was had to compulsory measures; and, in the autumn of 1917, orders were issued for the compulsory requisition of foreign securities owned by Germans within German territory.

In addition to this, a fairly active sale of German securities took place, in order to meet debts abroad.

It is difficult to estimate what the sum total was, but I believe that, taken all in all, \$1,500,000,000 is about the correct figure.

The purchases of paper marks and claims in terms of marks made by neutrals on speculative grounds doubtless also helped to meet the indebtedness arising out of our adverse trade balance during the War. As the German paper money and mark claims were rendered worthless by the collapse of the currency, this amount, which foreign countries lost by speculating in German marks, can be deducted from the debit balance. I believe that the amount is rather over- than underestimated at \$1,000,000,000. The result arrived at is a loss of about \$3,000,000,000 in the national wealth of Germany caused by the payment of imports during the War.

But the losses of capital inside Germany were much more serious. Germany's entire productive industry was occupied to an ever increasing extent, in meeting the needs of the War. The entire proceeds of German labor during those years was literally consumed in powder and smoke. Not only were our entire reserves of foreign raw materials exhausted, but, in addition, our whole supply of metal articles was almost entirely disposed of. Copper vessels were taken from the kitchens, the church bells were melted down, and all bronze and copper parts of industrial machinery were, as far as possible, replaced by inferior substitutes. Copper was torn from the roofs of houses and usable metal from lightning conductors at an enormous cost, out of all proportion to the value of the resulting metal.

But what was much worse was the extravagant use of coal and ore, entailed by the shortage of avail-

able labor and material, and the really disastrous effect on public and private means of transport, especially on the railways, due to the deterioration of all fixed and rolling stock.

During the War the German industries had been completely diverted to the production of war material and in this way, especially during the last years of the War, enormous war profits had been made, which were used in part for the construction of a big increase in plant.

But this apparent industrial prosperity was only a symptom of war; when the War was over, it became terribly apparent in Germany that a great quantity of plant had been built up which was quite useless for peace-time production, and thus a heavy drag upon our economic life.

On the other hand the plant for the production of peace-time goods had not only not been improved in any way during the five bad war years but had indeed deteriorated greatly. The consequence was that, on the credit side, the capital invested in industrial undertakings had much decreased, above all in effective value. Little comfort is to be found in the fact that individual plants on a huge scale, as for instance the artificial fertilizer factories, have proved productive in normal times and continue to have a favorable influence on our financial and commercial balance-sheet.

In addition to these heavy material losses, the loss in man-power must be borne in mind, as it exerted a terrible influence on the nation's future cultural and economic situation. I think that no more severe charge can be made against war, and that there is no consideration which makes it clearer to the thinking

mind and tender heart that war is the greatest curse and worst enemy of all races on earth, than a clear statement of the loss of man-power caused by the late War. I will not quote the figures of the other countries, equally impressive, but shall, following my theme, restrict myself to Germany. In Germany the war casualties were 1.8 millions killed and 4.3 millions wounded.

It neither is nor can be my task to describe the sum of human suffering represented by these figures (as for instance when we remember that more than 4,300 war-blind are still living in Germany); I will only remark, within the limits of my address, that this sacrifice of our youth on the field of battle represents a loss in German productive power which is difficult to estimate in figures but which at least approaches, in its effect, the neglected state of our productive plant.

And this is not all. Those who still survived in Germany were utterly exhausted. A physical exhaustion due to the years of privation caused by the blockade and a mental exhaustion caused, first, by the terrible awakening from the hopes of victory which were kept alive far too long by official propaganda and, secondly, by the hopeless situation which they found awaiting them on return from the scene of war and the revolution which broke out as a natural consequence of this situation.

Hence, the financial and economic balance at the end of the War may be summarized thus: The balance of trade had been adverse by at least twelve billions during the War; fresh capital had not accumulated; while, on the other hand, the value of our productive plant had been reduced by approximately

one-third. Germany's most important means of production, her man-power, had been partly destroyed, and that particularly in the age classes of the greatest importance for production. The stocks of raw material and the stores of reserve material were exhausted; the State was burdened with a new debt of over \$25,000,000,000 or about \$500 per head of the population.

A people which desired, in such circumstances, to free itself from an inflation which had already made considerable progress, would have required years of the most intensive and clear-sighted work and economy and, as the first condition, complete freedom from external and internal strife.

Instead of such tranquillity, what was really the situation in Germany in November, 1918? Her defeated army returned to a hungry homeland where all civic order had collapsed. Bolshevism was rampant on the eastern frontier and the danger of a moral infection of the whole German population was extraordinarily great, for hunger has always been the best soil for the endemic spread of fanatical ideas. In addition, the armistice conditions involved an unprecedented national humiliation which made one fear the worst from the definite conclusion of peace and caused in many cases a gloomy attitude of resignation.

In those circumstances the combating of inflation was not the care of the moment in Germany; no one gave any consideration whatever to this serious problem during those months when everything threatened to collapse. For even the fears of the conclusion of a peace which would ruin Germany's future had to be pushed aside in order that all avail-

able forces might be employed in saving Germany from Bolshevism.

There was only one really urgent problem of the moment, and the fate of the nation depended on its solution. Now that the old and decayed State, with its twenty effete dynasties, had broken down almost without an effort at resistance, the problem of the day became: Will it be possible to build up a new Germany on democratic lines or will the idea of Bolshevism prove victorious among the defeated, hungry and despairing people? There were days when it seemed hopeless to make a stand against the flood of Bolshevism which threatened to engulf Germany. But it was just at this moment of greatest need, when everything threatened to collapse, that the strength of the long-suppressed will of the German people for freedom and right made itself felt in an almost supernatural manner. At the time when the executive power had fallen into the hands of soldiers' and workmen's councils of a Bolshevik pattern, which to some extent imposed a tyrannical discipline intended by the leaders to develop into a Bolshevik régime, at this moment, I repeat, a group of courageous men who had not lost their belief in Germany's future, met together and demanded the suppression of the revolution by the summoning of a freely elected National Constitutional Assembly, an energetic step which entailed great personal risk.

That was the hour of the birth of the popular constitutional party in Germany which took the name of the Democratic Party. It recognized its historical mission to be that of providing the country with a safe constitutional legal foundation on the basis of democracy. This newly founded Democratic Party

won over the Social Democrats, already under the wise leadership of the future President Ebert, who was later to prove himself one of Germany's great statesmen. While the Bolsheviks caused sanguinary street fighting in Berlin and other parts of Germany, the lists for the National Assembly were compiled. I believe that the German men who then carried through the idea of a democratic state after the terrible defeat which the German people had suffered, will be rewarded by history with the same proud and beautiful expression of thanks which the Roman Senate in ancient times conveyed to the defeated consuls after a lost battle "*quod de re publica non desperaverunt.*"

Germany's leaders did not despair of the State, and so the construction of a new Germany was begun even while the flames of revolution were still flickering on every side.

The temper of the people during the elections to the National Assembly was one of despair. This was due in the first place to the fact that the blockade against Germany was maintained even after the armistice, so that consequently foodstuffs were imported into the starving country in quite insufficient quantities. The heavy mortality continued and it is easy to understand the bitterness and despair of the German people when, in February, 1919, the weekly ration of potatoes, which then constituted the principal foodstuff of the poorer classes, was reduced to five pounds, an amount which was quite insufficient from a hygienic point of view.

It is true that charitable organizations in neutral countries and in America were sending us help, for which the German people will be grateful for all

time; but all this assistance was only a drop of water on a hot stone, so long as the Allies did not abandon the procedure of compelling the acceptance of a dictated peace by the continuance of the blockade.

In such a state of affairs, is it not comprehensible that the radical elements in Germany should have looked to the East for assistance and that the German Bolsheviks, then known as Spartacists, should have believed their hour to have come?

Sanguinary insurrections in Berlin led to civil war and, in face of the greatest difficulties and sacrifices, it was only by the use of hurriedly collected troops that it was possible to overcome the Communist movement in Berlin, while temporarily abandoning other industrial centers to the radicals.

To a large extent my own home state, Saxony, where I was Finance Minister for the first time after the foolish Kapp *putsch* in the spring of 1920, was, for weeks, in the hands of the Communists, who blindly followed the leadership of a fanatical adventurer. The reason these peace-loving and hard-working Saxons joined the fanatics will be clear if one remembers that, a year after the conclusion of peace, there were many factory villages in that part of the country where not one woman of the working classes could be found who, on medical examination, weighed more than one hundred pounds.

A special danger-point had come into existence in Bavaria, where, in the spring of 1919, a Bolshevik Soviet Republic partly under Russian leadership had been proclaimed, and attempts made to establish relations with the simultaneously established Soviet Republic in Hungary under Bela Kun. Here, too, it was necessary to conduct a regular campaign

which proved exceedingly sanguinary—and all this occurred while the blockade was still in force and the armistice was being prolonged from month to month under ever increasingly severe conditions.

But, in spite of everything, the elections for the National Assembly had taken place, all men and women over twenty-one years of age having the same right to vote. The radicals had been reduced to a minority and, what was hardly expected, a non-socialist majority had been obtained, so that the Social Democrats entered a coalition with the Center and the Democrats. The result was that private property remained the inviolable basis of economic life and culture in Germany and the reconstruction of the country was not seriously imperiled by Bolshevik or socialist theories.

On August 11, 1919, the revolution had been mastered and a new legal basis for the German nation created by the acceptance of the new Constitution.

This new Constitution which adapted the great, free, and just principles of the American Constitution to German conditions differs materially in many points from the old monarchical Constitution of the German Empire, and is undoubtedly one of the freest democratic constitutions of the world.

It is true that Bismarck had already introduced the universal, equal, and secret ballot for the Reichstag in order to achieve German unity, but the real shortcoming, from a democratic viewpoint in old Germany was the Kaiser's power, for he, as King of Prussia, was quite free to choose his own Ministers, who could not be driven from office by any vote of non-confidence so that a very autocratic régime was rendered possible.

The new Constitution of August 11, 1919, on the contrary, put the German people's right of self-determination in the place of monarchical sovereignty. This is made quite clear in the very wording of the preamble. Whereas the old Constitution began with the words "His Majesty the King of Prussia, His Majesty the King of Bavaria" and so on, the new democratic Constitution begins: "The German people, united in its parts, has given to itself the following Constitution." This new Constitution, although, like all human handiwork, not free from faults and weak points, has proved itself a strong bulwark of democratic freedom in the eight years of its existence. I am firmly convinced that, as far as one can see, it will form a guarantee that Germany will not again leave the path which she first trod in 1919, namely, that of guaranteeing the internal freedom and equality of all Germans by the just application of democratic principles and by recognizing abroad the freedom and equality of all nations and demanding such recognition for herself.

The crushing of the revolution and the creation of constitutional conditions called forth fresh confidence in the German currency, at home and abroad, and provided the possibility of putting the national finances in order and arresting inflation by a speedy revision of the laws governing taxation. The collection of customs duties in gold was ordered as early as July 21, 1919. In September of the same year a beginning was made with the fiscal legislation, necessary for balancing the budget, in the form of an unusually severe act introducing the War Profits Tax, which went so far as to provide complete confiscation in the case of exorbitant profits.

But these measures were unable to exercise their full effect, for it became clearer from month to month that the war reparation payments with which the German people were to be burdened, contrary to the original Wilson program, were so enormous that their fulfillment was bound to entail the collapse of the German currency.

I shall speak about these reparation payments in detail in my next lecture.

The fate of the mark from this time onward was no longer dependent on measures taken in Germany, but depended completely on the development of foreign politics. The German currency reacted with automatic certainty to every act of violence of external policy, and such a terrible and hopeless state of affairs was reached that all efforts on the part of the German Government to balance the budget were brought to naught by the depreciation of the mark.

The burden of taxation might be raised ever so high, but as some time necessarily elapsed between the notification of the taxes and their collection, success was impossible owing to the further depreciation of the currency which had meanwhile taken place. Germany was, at this time, like a man chasing his own shadow in breathless haste.

It is true that there were certain breathing spaces when the drop of the mark, or, as it was incorrectly called in Germany, the rise in the dollar came to a standstill. These were the times when an economic solution of the reparation problem seemed feasible, as for instance in the months of April, May, and June, 1922, when the so-called Loan Committee was negotiating in Paris and it was hoped, not only in Germany but in the whole world, that, in this way,

the reparation question would be removed from the atmosphere of political sentiment to the sphere of economic consideration.

But the negotiations having been abandoned, under political pressure, and the representative of the German policy of conciliation, Minister Rathenau, having been shortly afterwards killed by fanatical Nationalist murderers, a new drop in the value of the mark began, so that, by the beginning of July, five hundred marks was paid for a dollar and, after the break-up of the London Conference of August 15, one thousand marks. An attempt to maintain the value of the mark by artificial means, after Rathenau's murder, met with only temporary success. After the Reichsbank had vainly sacrificed a fairly considerable part of its stock of gold and foreign currencies, it had to be recognized that the natural development must be allowed to continue and that the fall of the mark could not be arrested so long as the policy of violence continued. And so, when it became daily more evident that France meant to carry out the threat of occupying the Ruhr area, the mark could no longer be controlled. After the French and Belgians had occupied the Ruhr on January 11, 1923, the dollar rate rose to fifty thousand; that is to say, the mark had sunk in a few months to less than one hundredth part of the value which it had when Rathenau was murdered and to less than a thousandth part of its pre-war value.

This fall was not justified by the internal conditions of the German currency, for the bank note circulation was at that time only about two thousand billion, which at a dollar rate of fifty thousand, represented merely a sum of \$40,000,000, while the gold

and foreign currency reserves of the Reichsbank were equal to several times this amount. The low value of the mark led to the expression of the expectation of international speculators that Germany would hardly survive the occupation of the Ruhr as a national entity and that, in any case, her currency was hopelessly ruined.

In these circumstances, the German Government decided upon bold action in support of the mark, under the leadership of the then Finance Minister Hermalme. The moment for this was undoubtedly well chosen owing to the undervaluation of the mark. Early in February, 1923, the Reichsbank began to part with its foreign currency, and was actually successful in bringing down the dollar rate from fifty thousand to twenty-three thousand five hundred which intimidated the speculators to such an extent that they brought the rate down to twenty thousand a few days later by what they themselves sold.

It was possible to maintain this rate until the middle of April. But as no clearing up of the political horizon could be detected and the French, on the contrary, proceeded to install themselves even more firmly in the Ruhr, destroying not only German economic life but also private property and, above all, seizing billions of Reichsbank notes, the last bold attempt of the Reichsbank to save the German currency had to be abandoned. The action in support of the mark collapsed on April 18, 1923, after the Reichsbank had vainly sacrificed about \$100,000,000 of its shrunken supplies of gold and currency.

It is true that one more effort to support the mark was made in July, which was accompanied by severe regulations regarding the rate and purchase of for-

eign currency; but this attempt also failed and the mark sank indefinitely. By the beginning of July a dollar rate of one hundred and sixty thousand had been reached and by the end of the month the rate was one million.

From this time onward, control was quite impossible. I would like to explain how rapid the pace of the drop in the mark was by reference to one fact, namely, that even the printing presses were unable to keep pace with the demand for notes, the whole paper-money system being thereby rendered an absurdity. Can there be any more striking proof of the cumulative ridiculousness involved in this printing of worthless paper with senseless figures than the fact that, at that time, all over Germany people were printing their own money—the so-called “emergency money”—and that over three hundred paper mills were working at the highest pressure to produce paper for the notes of the Reichsbank alone, and further that in one hundred and fifty printing works, approximately two thousand presses were running day and night to print those notes, that is, as people then believed, to convert the paper into money?

It is only natural that this nonsensical process sucked all purchasing power out of the mark. The most terrible thing occurred that can happen to a civilized state, namely, its legal tender ceased to be recognized by its own nationals; the repudiation of the mark began; only those who have experienced it, can appreciate what that means. It means that the agricultural districts refuse to furnish the towns and cities with food supplies, that the retail shops decline to part with their goods against payment in the

national currency, that no standard can be found to decide the amount of wages, that those "living on their means" have ceased to have any means, that they are reduced to the bitterest penury and unable to purchase a morsel of food to stay their hunger.

Once more hunger riots broke out, and, in September, a state of siege had to be declared.

Once again, too, the specter of revolution loomed up. In Saxony and Thuringia bolshevistic squadrons were formed; communistic Ministers received portfolios in the Saxon Government, and though they did, indeed, take the oath of loyalty to the Constitution, they openly called for a communistic revolution.

On the other hand, as so often happens in the world's history, the terrors of the Communist régime through which Bavaria had passed, now led, in combination with new circumstances, to excesses in the reverse direction, so that the Nationalists, under the fascistic leadership of Hitler, started an opposition *putsch*, and Germany saw herself divided into two armed camps.

In the Rhineland, armed crowds, consisting mainly of paid ruffians, and calling themselves Separatists, proclaimed the secession of the Rhineland from the Reich and obtained the upper hand in a part of the territory occupied by the French, whereas the districts under British occupation remained perfectly tranquil.

Never, not even in the year 1919, had Germany been so exposed to the dangers of Bolshevism as in the days when the French, by the occupation of the Ruhr Basin, held in their hands the heart of the German economic organism, and, in the unoccupied

territory, the distress was so great that even well-balanced minds fell a prey to the influence of agitators.

And yet, in those days, when everything seemed lost, the greatest wonder took place that German economy has ever seen. Under the whip of the fiercest distress and led by a few great men who had not lost their faith in their country, the German people pulled themselves, out of the swamp, as it were, by the hair of the head like Munchausen in the fable, and found a firm footing under their feet. This firm footing was provided for them by the stabilized mark; this deed of salvation, due mainly to the Finance Minister Luther and Dr. Schacht, the Currency Commissioner—an office created *ad hoc*—was the remarkable feat known as the “Miracle of the Rentenmark,”—a feat that will ever remain one of the most notable in the history of political economy.

In what does the miracle of the Rentenmark consist? In a simultaneous attack upon the inflation at three points, namely, the currency itself, the State finances, and industry; as also in the energetic, almost cruel application of resolute measures by that highly gifted man, Dr. Luther, into whose hands Parliament had entrusted the dictatorial powers of the Emergency Act.

Dr. Luther himself has defined the function of the Rentenmark in the following manner: the currency is like the roof of a house whose foundations are balanced state finances and whose walls are economically sound industries. In November, 1923, we had in Germany neither a balanced budget nor a sound economy; the roof, in the shape of the new currency, lacked its supporting walls; and since the building

had to be begun at the top, a scaffolding was necessary till the walls had been built: that scaffolding was the Rentenmark.

One must never overlook the fact that the Rentenmark was only an auxiliary currency; it was not legal tender, and no fixed rate of conversion between it and the old paper mark existed; hence it was, in fact, nothing but money based on trust, money based on hope; and its success can be explained only by the fact that the German people turned suddenly from the miseries and horrors of inflation to clutch at the Rentenmark as at a straw.

It was, in truth, nothing but a straw. The political economists who opposed the project could, with perfect justice, point out that the money of the notorious John Law swindle in the eighteenth century, as well as the *assignats* of the French Revolution, were, in fact, founded upon landed property, just like the new Rentenmark.

For the Rentenmark had no metal covering; its sole real guarantee consisted in its being exchangeable for mortgage bonds the basis of which, again, was a general lien upon the entire agricultural and factory property of the country. It was a guarantee which, highly problematical even for home purposes, was utterly unfitted for international intercourse. It is interesting to peruse the arguments against a currency based upon mortgages used by such a brilliant expert in monetary affairs as Max Warburg when addressing the German Bankers' Congress in the autumn of 1920. Among other things, he said: "A mortgage does not satisfy the main requirement of a currency reserve, *i.e.*, the so-called backing of the notes must be fitted to act as an international means

of payment, as a regulator of exchange rates. Herein lies the significance of gold as a backing for notes, so long as other countries remain willing to take gold in payment. But this function does not pertain to mortgage backing. Money issued against landed property is not readily convertible into a fluid and mobile commodity, but at most into an hypothecation of rights whose value depends upon the security of the land, upon the real property market, etc. This proposal therefore appears anything but advisable."

When, therefore, the project of the Rentenmark was opened to discussion in October, 1923, almost all the theoreticians, and even such practical parties as the Central Association of the German Wholesale Trade and the Central Association of the German Banks and Banking Businesses, adopted a distinctly adverse attitude toward the plan, at any rate, as originally drafted by Helfferich.

And yet the experiment succeeded, notwithstanding all its inherent theoretical faults, because of the energy of Luther and Schacht, coupled with the sound instinct of the German people who, convinced by inflation that a stable currency is essential to the life of a nation, regarded the new money as its savior and accepted it with an almost extravagant measure of confidence despite its lack of backing.

As a result, the speculators who, stiffened by their gains in the inflation and failing to reckon with the important imponderable factor of the popular will, scented fresh possibilities of enrichment in speculation against the Rentenmark, were this time defeated. It proved possible to maintain the proposed rate of one thousand billion paper marks = one Rentenmark

= $1\frac{1}{2}$ of one dollar till the Rentenmark scaffolding could be removed because the foundations and the walls of the new German house were strong enough to support the roof in the form of a new Reich currency.

How the stabilization was carried out and what difficulties had to be overcome, as well as the condition of the German people and of German economy after the inflation had passed—all this I shall have to describe in my third lecture.

I must now leave the line running from the properly funded pre-war German mark, through the unhappy ratio of one dollar for four thousand two hundred billion paper marks, to the new Reichsmark, and must traverse the line running parallel with the first of those and leading from the Fourteen Points of President Wilson through the dictated Peace of Versailles and the London Ultimatum up to the Dawes Plan.

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LECTURE II

REPARATIONS FROM THE ARMISTICE TO THE DAWES PLAN

ON January 8, 1918, President Wilson, in a message to Congress, publicly announced his program concerning the conclusion of peace, a program which, under the name of the "Fourteen Points," has since played such an important rôle. On October 3, 1918, the last Imperial German Government, then recently formed under the Chancellorship of Prince Max of Baden, accepted this program as a basis for peace negotiations and requested President Wilson to bring about an immediate armistice on land, on sea, and in the air.

In Wilson's Fourteen Points a claim for reparation of the war damages was formulated to the effect that the occupied territories must be restored; and, on November 5, 1918, in a note sent by Secretary Lansing of the State Department on behalf of the Allied and Associated Powers, this restoration was interpreted to mean reparation for "all damage done to the civilian population of the Allies and their property by the aggression of Germany, by land, by sea, and from the air."

This interpretation was accepted by Germany, and I must, as a national of that defeated State, declare quite frankly that the claim appears to me as just as it is moderate and that it harmonized with the sense of justice of vast numbers of Germans. I recollect vividly the ideas which, at that time, we of

the younger school of German politicians cherished; we had ever been opposed to imperialism and, taking to heart the terrible lessons of the War and wishing the political atmosphere which surrounded the peoples of Europe to be speedily purged of hatred, we planned schemes on the basis of the American conditions whereby fresh German hosts were to proceed to the occupied territories, but, this time, not for bellicose purposes and to effect destruction; no, they were to be labor volunteers who, with material sent from the German homeland, were to repair as rapidly as possible the destruction wrought by the War.

At that time, we were so optimistic as to believe that this reparation army provided by the new Germany was destined to demonstrate that, in Europe, the will of the peoples had definitely put an end to the era of war and destruction.

Recalling that frame of mind of the German people and yet recognizing fully that it failed to appreciate both the deeper forces of excited passion and the feelings of the victors, I must nevertheless point out, in this year 1927 of the Christian era, what an endless number of difficulties would never have arisen, either for Germany or for the world, if, at Versailles, Germany's reparation obligations had been fixed in conformity with President Wilson's proposal and the note of State Secretary Lansing.

But, upon the collapse of Germany, the settlement of the reparation question took quite a different course. Even in the negotiations on the armistice conditions of November 11, 1918, the principle laid down in Lansing's note was abandoned for a proposal of Clemenceau's. It is quite affecting to read in

Peaceless Europe, written by the Italian Prime Minister, Francesco Nitti, in 1921, how Clemenceau's proposal came to be adopted in the armistice conditions. Nitti writes:

It must be expressly stated that the most difficult decisions, both in the Armistice and in the Peace Treaty were, so to speak, casually made. The most important decisions were always influenced by slight and seemingly unessential concessions. On November 2, 1918, the reparation question was, as Tardieu states, settled quite incidentally. It is worth while to reproduce from his book the passage quoted from the protocol:

"*M. Clemenceau*: Je voudrais revenir maintenant sur la question des réparations des dommages. On ne comprendrait pas chez nous, en France, que nous n'inscrivions pas dans l'armistice une clause à cet effet. Ce que je vous demande c'est l'addition de trois mots! Réparation des dommages, sans autre commentaire."

This proposal evoked a short debate, in which Bonar Law at first objected; but ultimately the protocol states laconically: "L'addition 'Réparation des dommages' est alors adopté."

These three momentous words, quite casually adopted as Nitti says, gave rise, little by little, to those demands which gradually claimed the repayment of all war costs in place of reparation for the damage done to the civilian population, which was all that Wilson's program required.

On December 11, 1918, for example, Lloyd George, speaking at Bristol, assumed this standpoint and claimed for Great Britain alone eight billion pounds sterling as war damages.

The American Delegation recognized at once the danger lurking in these extreme demands. They con-

sequently undertook a bitter struggle in favor of the Wilson program. So convinced were they of the world's economy being imperiled, that they argued with an energy and decision which threatened to cause an open rupture between America and the Allies. In the end, however, Clemenceau and Lloyd George succeeded in breaking down Wilson's opposition and inducing him to concede that military pensions and other annuities were to be capitalized and recognized as claims to be paid by Germany to the victors.

By an utterly arbitrary interpretation, this compromise could, indeed, be construed as conforming, at any rate verbally, with Lansing's note; but the Treaty of Versailles vastly outdid this compromise by the introduction of Article 231 which made Germany responsible for all war losses suffered by the Allies. On account of Germany's incapacity to pay, the theoretical claim was limited in practice to the damages specified in Article 232, in which, *inter alia*, the pensions and all other expenses for the military and their families are enumerated. The amount of these claims was to be determined by a Commission and announced to Germany by May 1, 1921.

Previously, Germany was to pay by May 1, 1921, an installment of twenty billion gold marks and, at the same time, to transfer to the Reparation Commission one hundred billions in bonds.

In addition, the payments in kind to be made by Germany were fixed, the principal items being:

1. All merchant ships of 1,600 tons gross and upwards; one-half of the ships between 1,000 tons and 1,600 tons gross; and one-quarter of all fishing boats.
2. Supplies of animals. Here I must state that the de-

mand for 140,000 milch cows to be delivered within three months evoked great bitterness in Germany, as there was not sufficient milk to meet the needs of the sick and of the infants, although the charitable help of the Americans and the neutrals somewhat mitigated the distress.

3. Delivery of machinery, tools, etc.
4. Coal and products of coal to a total of 43½ million tons per year.
5. Chemicals to a total of 50 per cent of the stocks held in Germany.

All this, although, in pursuance of the terms of the armistice, the materials coming from the occupied territories, cash assets, and securities, which, being restitutions, were not credited to reparation account, had already been restored and enormous quantities of war material, such as five thousand locomotives, one hundred and fifty thousand railway vans and five thousand motor lorries had been handed over.

The reparation account was to be credited with the German private assets held abroad—as far as they were not used for compensating claims arising out of pre-war debts, of German exceptional war measures and of neutrality losses—as well as with the value of the Saar coal mines to be ceded to France and a few other small items.

But, over and above these obligations, Germany was to shoulder other heavy burdens. She was to hand over to France, *gratis*, and without any credit in the reparation account, all the railways in Alsace-Lorraine, together with the rolling stock; and she was to transfer to Belgium all her State property in Eupen and Malmedy. She had also, from November

11, 1918, onwards, to bear all the costs of the armies of occupation, and, finally, to meet, by way of the clearing offices, all the private debts owed by German nationals to nationals of the Allied and Associated Powers.

Finally, she had to accept responsibility for indemnifying German nationals for the confiscation of their property by the Allied and Associated Powers. In reference to these stipulations concerning the confiscation of private property, I feel constrained to say that, in my view, there can be no worse relapse than this into the barbarism of an almost forgotten past, in which victorious armies and victorious countries enriched themselves by the removal of the private property of the vanquished.

That, during war, provision is made, by means of sequestration, to prevent enemy property from being employed to strengthen the enemy's financial position appears to me quite a comprehensible war measure. But that anyone, after the cessation of hostilities, should confiscate the private property of foreigners, instead of regarding it as a duty of honor to treat it with all the care of a faithful trustee and then to restore it to the private owner, seems to me such a questionable and serious breach of the principles of private ownership that all states which, in contradistinction to Bolshevism, see in private ownership the foundation of civilization and of cultural and technical progress should set their faces sternly against such a proceeding, in order that no precedent be created for future wars—a precedent calculated to jeopardize most seriously the free movement of capital and the sacredness of private property.

Hence, I consider that the American nation is going to do a great service to civilization by treating the question of the release of private property seized during the War in a fair, broad-minded, and practical, common-sense manner.

But to return to the Treaty of Versailles. Notwithstanding the energetic protests of the American Delegation, the total burden to be borne by Germany was not reduced to figures; it was merely arranged that the Reparation Commission should inform Germany of the amount by May 1, 1921, and state the installments in which it was to be paid within thirty years.

What sums, however, the victors expected from Germany may be gathered from a perusal of the Preliminary Project presented to the Supreme Council by the French Minister of Finance, M. Klotz, on April 12, 1919. Klotz proposed an immediate payment of twenty-four billion gold marks and an annuity beginning with eight billions in the second year after the conclusion of peace and rising annually by 2 per cent.

I believe history has never known another case of a vanquished people being forced, more than six months after the conclusion of an armistice, to sign a blank check which the victors might fill in according to their own sweet will.

On May 29, Germany had addressed to the French Prime Minister, M. Clemenceau, a note in which it was proposed to pay, by way of reparation, twenty billion gold marks by May 1, 1926, and finally a total of eighty billions. In this note, the passage referring to reparation, as originally claimed by Wilson, runs thus: "Germany is prepared to devote to the resto-

ration all her economic forces; she desires to coöperate actively in the reconstruction of the devastated districts of Belgium and France."

I quote this passage word for word because it illustrates clearly the temper of the new Germany as I have already described it. We believed, at that time, that we could best assist in the reconstruction of Europe—not merely in a material but also in a moral sense—if, by the use of organized German labor, we repaired as quickly as possible and before the eyes of the whole world the damage done by the German armies during the War. That was the reason that Germany formed a special Ministry for Reconstruction and that the clause of the Treaty of Versailles requiring two hundred thousand tons of shipping to be built annually in German yards and handed over to the Allies was welcomed as a fair method of indemnification.

But all German counter-proposals were knocked on the head on July 16, 1919, by the Covering Note of President Clemenceau; and the German Government found themselves face to face with the momentous question whether they should accept the Versailles dictation just as it was or resume hostilities.

In discussing the Treaty of Versailles, I have, of course, confined myself to the reparation clauses as any discussion of the rest of the Treaty would exceed the scope of my lecture. Still, I may say, in passing, that I believe any impartial observer, who should consider to what extent the Treaty as a whole deviates from the just and broad-minded attitude of Wilson's Fourteen Points, will inevitably come to the conclusion that Europe has been plunged into a slough of misery and into almost inextricable diffi-

culties just because the fair principles of the American proposal were thrust aside to make way for the wishes of the victor states.

So, too, the forcing of Germany to admit her sole responsibility for the War, which, according to my conscientious conviction, constitutes an historic untruth, was a violation of conscience such as had never before been demanded by any peace treaty.

Nevertheless, Germany signed. She was bound to sign; because the enemies' armies, ready for immediate advance, stood, not on the frontier, but right in her own territory. If Germany had not willingly entered the Caudine Forks, war would have broken out once more, and I am convinced that things would have ended in the triumph of Bolshevism in Germany as well as elsewhere.

But let us resume the reparation question. The Treaty of Versailles placed the settlement of the whole matter in the hands of a Reparation Commission. That Commission was endowed with exceptionally wide powers, and was to act independently of the governments of the victor states till the reparation debt was completely settled. It was not to "be bound by any particular code or rules of law"; it was to "be guided by justice, equity and good faith."

In all sittings of the Commission, the representatives of America, Great Britain, France, and Italy, and, in general, Belgium, were to participate and have the right to vote.

I feel convinced that Germany has suffered no greater mishap since the War than the fact that, in consequence of the American refusal to ratify the Treaty of Versailles, the American representative officially resigned from the Reparation Commission.

I believe that, for the benefit of the whole world, the economic insight displayed by the Dawes Plan would, at a much earlier date, have carried the day, if a representative of the American nation had exerted decisive influence in the Reparation Commission. As, unfortunately both for Germany and for the whole world, this was not the case, the Reparation Commission, despite the best efforts of certain delegates to do objective work, became the shuttlecock of political passions, so that, in the end, its decisions were dictated by the politics of the day.

The first attempt to determine the aggregate obligations of Germany was made at Boulogne by the Prime Ministers of the Allied States on June 20, 1920.

On that occasion, the total sum was fixed at two hundred and sixty-nine billion gold marks payable in forty-two annual installments beginning with three billions in May, 1921, and rising gradually to seven billions. Such was the attitude of the Allies at that time; it led to the Spa Conference of August, 1920—a conference dominated by the war psychosis; and the reparation problem made not an inch of progress. True, the Allies came to an agreement as to the distribution among themselves of the German reparations—the so-called Key of Spa—but the amount of the German indebtedness remained unsettled.

The Financial Conference at Brussels in the autumn of 1920 and the Conference of Experts in December, 1920, to discuss mainly the question of a provisorium led to the Paris Conference of January 29, 1921. At this last Conference, the French Minister of Finance, M. Doumer, demanded the fixing of the German debt at two hundred and twelve billions

to be paid in annual installments of twelve billions. In the end, the Allies agreed among themselves to the following annuities:

From May 1, 1921, onwards:

For the first two years, two billions per year,
For the next three years, three billions per year,
For the following three years, four billions per year,
For the next following three years, five billions per year,

and for another thirty-one years, six billion gold marks per year, in addition to all which, 12 per cent of the value of the German total exports was to be paid over.

I need not say, that this utterly impossible scheme was rejected both by the German Government and by all shades of German public opinion. The temper of both parties had grown exceedingly irritable, especially as, meanwhile, the question of the coal deliveries had become acute. Hence, there followed in March the London Conference at which Dr. Simons, the German Foreign Minister, submitted, at the outset, the proposal of his Government that the total sum of the German indebtedness should be fixed at fifty billions; but as this proposal met with a brusque rejection, he suggested a provisorium.

The Allied statesmen, however, declared that, failing Germany's acceptance of the Paris resolutions by March 7, the Allies would resort to sanctions; namely, they would proceed to occupy the cities of Düsseldorf, Duisburg, and Ruhrort; they would also retain a portion of the value of the German imports, would confiscate the German customs in the Occupied Territory, and erect a customs frontier between that territory and the unoccupied territory.

And as Germany had not submitted to this dictation by March 7, Marshal Foch marched, during the night, across the boundary fixed by the Treaty of Versailles, and occupied Düsseldorf, Duisburg, and Ruhrort.

That was the manner in which, at that time, people imagined they could solve questions of world economy. The visible result was a fresh fall of the mark, which, in its turn, increased the difficulties of the reparation problem. On March 26, the Reparation Commission informed the German Government that twelve billions were to be paid by May 1, *i.e.*, within six weeks; and further, one billion in dollars, sterling, and francs, by May 23, the remaining eleven billions to be provided in the form of commodities or securities, or by the issue of a loan. A few days later there came a fresh ultimatum requiring the entire stocks of gold and silver held by the Reichsbank to be transferred to the Occupied Territory.

You will, I feel sure, agree with me that, today, with our present clearer view of the economic situation, it is quite impossible to understand how such a demand could have been seriously discussed. And yet, as by May 1, the twelve billions were not forthcoming, the Reparation Commission informed the Allied Governments that Germany was in default as regards the payment of twelve billions. I shall have to speak of this point again later, inasmuch as even the question of payment or non-payment is extremely debatable. Germany, herself, holds the view that considerably more than the twenty billions demanded had been transferred by payments in kind, whereas the Reparation Commission declined to

credit more than eight billions to Reparation account.

Next followed a fresh Allied ultimatum, the so-called London Scheme of Payment of May 5, 1921. This scheme fixed the total indebtedness at one hundred and thirty-two billions, of which twelve billions was to be provided by July 1, 1921, in the shape of gold mark bonds A, and, by November 1, 1921, thirty-eight billions in gold mark bonds B, and eighty-two billions in gold mark bonds C; all to bear interest at the rate of 5 per cent plus 1 per cent sinking fund, the reservation being made that the C bonds were not to be issued till the German payments sufficed to meet the interest and sinking fund service of these bonds.

Germany was to pay current annuities amounting to two billions in gold plus 26 per cent of the value of her exports till the amortization of all the bonds was complete; the first half-year's installment of one billion was to be paid immediately in gold, foreign bills or German three months' Treasury bills endorsed by German banks.

The German Government was given six days to accept this ultimatum; if, by then, it had not been accepted, various military sanctions by land and by sea would be resorted to, including the immediate occupation of the Ruhr Basin.

Just as at the time of the peace dictated at Versailles, Germany once more had to face the question of whether she should accede, without negotiations, to an ultimatum which her Government, all her economic circles, her entire press, and every political party felt to be unjust and unfeasible, or whether

she should allow her territory to be occupied by foreign troops.

And, exactly as happened in the summer of 1919, the decision was in favor of submission. By a small majority, the Reichstag voted for acceptance of the ultimatum, and it was signed by a new Cabinet formed under Chancellor Wirth.

The billion demanded was obtained by the purchase of foreign bills and was actually paid by August 31, 1921. But this settled the fate of the German mark. For the first time, the exchange rate fell to 100 marks to the dollar; and the havoc wrought in German economy and the German Treasury rendered rapid inflation inevitable. By November, the mark possessed only one-fifth of the purchasing power it had enjoyed when the London Ultimatum was signed. It was clear that the further payments to which Germany was obligated were bound to end in the utter ruin of her currency.

In the autumn of 1921, John Maynard Keynes computed that, with automatic certainty, Germany was bound to default in her payments somewhere between February and August, 1922.

In these desperate circumstances, the German Government made an attempt to obtain a loan of one billion gold marks in London. The Governor of the Bank of England declined with the very fitting observation that "in view of the conditions which determined the obligations of the Reich to the Reparation Commission in respect of payments during the coming years, neither a long-term German loan nor a short-term bank credit was obtainable in England."

After this refusal, the German Government de-

cided, on December 14, 1921, to apply for a moratorium.

As the German purchases of foreign bills caused obvious disruption, not only in the German currency but in the other currencies of Europe, the Supreme Council of the Allies resolved to rediscuss the reparation problem in January, 1922, and to invite the German Government, then represented by Dr. Rathenau, to participate in the discussion.

In consequence of the fall of Briand, the Conference broke up without results; nevertheless, the Reparation Commission decided, on its own initiative, to modify the scheme of payment in such a way that thirty-one million gold marks should be paid every ten days.

These payments were made, but with the natural result that the mark sank further and further.

Although the heads of other Governments were present, Poincaré, who had succeeded to power in France on the fall of Briand, did not participate in the new Conference convoked at Genoa; and that Conference proved a failure.

Meanwhile a Loan Committee of the Reparation Commission met on May 24. This Committee, of which J. Pierpont Morgan was a member, did excellent work. But, on June 1, it resolved to enquire of the Reparation Commission whether, in its proceedings, it was to regard Germany's reparation debt, as fixed in London, as unalterable, or whether it had a free hand to consider other solutions. This resulted in its labors being knocked on the head by high politics. Poincaré, excited to the utmost by the action of the Loan Committee, made the following declaration in the French Chamber:

Even on the part of the Reparation Commission—or parallel with it—I see at this hour the most dangerous machinations in progress against us, with a view to making the international loans dependent upon a fresh reduction of our claims. This morning, on my responsibility, as head of the Government, I have informed the French delegate of the Reparation Commission that he may not agree thereto.

Hereupon, in spite of its excellent work, conducted for the first time on economic principles, the Loan Committee had to put an end to its activities.

Poincaré's policy became clearer and clearer. He was obliged to admit—no expert in the world questioned it at that time—that Germany needed a moratorium; but he was willing to grant it only against so-called "productive pledges." It became clearer, month by month, that the French would march: the war clouds loomed afresh over Germany. Hence a desperate collapse of the mark; by November, 1922, ten thousand Reichsmarks had to be paid for one dollar.

Fresh German proposals handed over on November 4 and December 9, 1922, and offered on January 1, 1923, failed to stem the tide. The Paris Conference held in January, 1923, was rather a dispute among the Allies than one between the Allies and Germany. French and Belgian troops marched into the Ruhr District. As Germany was said to be in default as regards the delivery of wood—more particularly, telegraph poles—the Reparation Commission, despite the protests of the British delegate, Sir John Bradbury, recorded that Germany had committed a culpable default in regard to her obligations; and, on January 9, once more against the vote

of the British delegate, a culpable default in the deliveries of coal was recorded by the Reparation Commission. Both were insignificant matters which, with mutual good will, might have been easily and quickly settled.

But they sufficed to provide Poincaré with a formal reason for carrying into execution the long-prepared raid of the Ruhr.

The German Government, possessing no military means of repulsing what it considered an illegal inroad, was forced to restrict itself to a solemn legal protest. The German ambassadors to Paris and Brussels left their posts: what was practically a state of war again ensued.

I will not go into details concerning the conflict on the Ruhr which Germany had to conduct, not with arms, but by passive resistance. I will not describe the whole course of this unhappy year in post-war European history with all its misery and suffering. Suffice it to say that Germany once more collapsed, and with her collapse, the currency, after an initially successful attempt on the part of her Government to prevent it, definitely and irretrievably lost all appreciable value.

In my first lecture, I described how necessity brought to the fore in Germany the men who, by the miraculous creation of the Rentenmark, stabilized German currency and thus saved their country from economic ruin. I have now to describe how, at a time of similar need, the Experts' Commission forever associated with the name of Charles G. Dawes, propounded an economic solution of the reparation problem, and thus ensured success in the stabilization of the mark.

As the basis for the cessation of hostilities was created by Wilson's Fourteen Points, so the movement toward the conclusion of financial peace also proceeded from America. The impulse was given by the speech of Secretary Hughes of the Department of State at New Haven on December 29, 1922. In that speech, he suggested that a committee of international financial and economic experts should study Germany's capacity to pay reparations.

But, this time, the American idea—not turned topsy-turvy as in the case of Wilson's Fourteen Points—was, despite the great obstacles which lay in the way, ultimately realized.

On May 2, 1923, when the Ruhr struggle was at its height, the German Government suggested the American proposal; it was rejected by Poincaré in the brusque manner. Consequently, the disruption of German economy and the German currency went on apace. Then came the renunciation of the policy of resistance in the Ruhr and the German Government once more requested the Reparation Commission to institute a scrutiny of the economic resources of Germany and of her capacity to pay. This time, the Reparation Commission agreed; it resolved, on November 30, to appoint two committees of experts. One, under the chairmanship of McKenna, was to study the question of the so-called flight of capital from Germany, which, owing to the world-wide expansion policy of Stinnes based upon inflation profits, formed, at that time, the principal subject of public discussion; while the other, under the chairmanship of Charles G. Dawes, was to "report upon the means of balancing the budget of Germany and

the measures to be taken to stabilize its currency.” The latter met in Paris on January 14, and, in less than three months, performed a task which, in my opinion, is to be classed as one of the finest performances in the whole history of economics and finance. All of us in Europe, blinded by years of political hatred and domination, failed to see a way out of the wood; we had lost the courage to believe that anything would come of this Committee’s report and imagined its interesting matter would simply be placed *ad acta* by the political dictators. But the courage, the freshness, and the expert knowledge of the men who went to work in January, above all of the two American delegates, was so new and so exceptional for Europe, and the results of their labors were so convincing, that the great task which was to liberate Europe from the nightmare of new wars proved successful. As early as April 9, 1924, the reports of the Committees of experts were handed to the Reparation Commission, and shortly afterwards made public. Barely three weeks later, the reports were officially endorsed by Great Britain, Belgium, and Italy; whereas Poincaré, one day later, avoided all formal agreement and expressed everything under complete reservation.

But this time destiny was on the side of the friends of peace and conciliation. On May 11, the French elections resulted in the defeat of the Nationalists and a majority for the Cartel of the Left; and, after a short interlude played by Millerand, Poincaré was replaced by a sincere friend of conciliation in the person of Herriot.

A conference was convoked in London. It met on

July 16, and, on August 5, a German delegation led by Marx, Stresemann, and Luther arrived. The Conference agreed to the Dawes Plan, and fixed August 30 as the date for its signature, the German Government having undertaken to do all, on its part, to get it accepted by the Reichstag.

That acceptance came about on August 29, but only after a very severe struggle which threatened to prove fatal, especially as, owing to the constitutional modifications involved in the transfer of the Reich railways to a joint-stock company, a two-thirds majority was requisite. Nevertheless the bill was finally passed, which enabled Germany to ratify the arrangement within the appointed time; one day later, on September 1, 1924, the Agent General for Reparation Payments *pro tem.*, Owen D. Young, was able to enter upon his duties.

The rapidity with which it was possible to put the plan into force was ascribable to two fortunate circumstances. One of these lay outside the sphere of the experts' influence: it was the fact that, in the three countries chiefly concerned, France, Great Britain, and Germany, the political helm was in the hands of men who, recognizing the terrible calamity into which War and the occupation of the Ruhr Basin had plunged Europe, were sincerely desirous of effecting a quick conciliation; they were likewise untrammelled by any of those red-tape tendencies which have so often worked mischief in the governments of European countries and might well have twisted and retarded the great work of the Dawes Committee.

The second circumstance was due to the remarkable foresight and energy of the Committee of Ex-

perts themselves. At the end of their Report they wrote: "We regard our report as an indivisible whole. It is not possible, in our opinion, to achieve any success by selecting certain of our recommendations for adoption and rejecting the others."

In this way no room was left open for higgling and haggling, for compromises and concessions, which might destroy the spirit and meaning of the whole, as Wilson's Fourteen Points were dulled by the Treaty of Versailles.

Now, in what did the greatness and the novelty of the Dawes Plan consist? It was, in the first place, the fact that the spirit of economic thought and fair and considered reason took the place of violent and egoistic politics, a fact which, in itself, is sufficient to explain the success. But, beyond this, the plan is characterized by an exactitude of method, which, for the first time, provided practical data for forming a proper judgment on the whole problem; finally—and this was perhaps the decisive factor—Germany was only required to pay in to the Agent General's account a definite sum in Reichsmarks, *i.e.*, in the currency of the country, while the question of the transfer abroad was left to the Agent General, who in this matter had to avail himself of the services of the German Government and the Reichsbank.

Only later, in dealing with the German economic situation and the German balance of trade, shall I be able to discuss this question of transfer. For the moment, let me merely state that the extraordinarily gifted compilers of the Dawes Plan were aware, from the outset, of the difficulties besetting this question, and that they, even at that time, envisaged the possibility that, without jeopardizing the Ger-

man currency—a thing which it was essential to avoid—it would be impossible to transfer abroad the sums paid in German currency. Hence it was provided that the payments of the German Government should cease of themselves whenever the funds accumulating to the credit of the Agent General and appearing to the Transfer Committee incapable of being transferred should have reached the sum of five billion gold marks.

Moreover, the Report itself says: “Experience, and experience alone, can show what transfer into foreign currencies can in practice be made.”

I shall, in a later lecture, take the opportunity of discussing this problem in detail.

In Germany people of all expert circles were well aware that the burdens placed upon us by the Dawes Plan and the pressure of taxation thereby rendered necessary were excessively heavy and would involve very great perils for the economic and the political situation of the country. But the Germans who desired conciliation were in the majority then and will, it is to be hoped, remain so for all time. The feelings with which they greeted the Dawes Plan were those of sincere confidence in its fairness and impartiality and of loyal determination to coöperate in the scheme. I believe I can best illustrate the spirit animating these circles by quoting the speech made by the President of the Reichsbank, Dr. Schacht, on October 31, 1924, at the luncheon given on the occasion of the first meeting of the German Ministers and the members of the General Council of the Reichsbank with the foreign representatives under the Dawes Plan. Dr. Schacht said:

It is a great honor for the President of the Reichsbank that today's gathering is being held in these rooms; it is a gathering to which one cannot deny historic significance. It is the first time for more than ten years that representatives of eight civilized nations have met to overcome in a spirit of amiability the great differences and divergencies hitherto existing. The desire of the German people for reconciliation and peace will be promoted by the fact that this coöperation takes place in a matter in which the German people can show performances as great as those of the other nations. What is the intellectual content of the coöperation which has found expression in the Dawes Plan? It is the replacement of the old methods of diplomacy and war by a new method which endeavors to solve the difficulties of human society.

These difficulties are manifold. There is, for one thing, a national difficulty inasmuch as every people must have the wish and the natural right to unite in a national entity all those who speak its language, live its habits and cherish its common traditions. Another difficulty is a social one, inasmuch as every one who will and can work has the right to an adequate subsistence which shall enable him and his children to share in the progress of material civilization which is a condition of intellectual civilization.

In the new method of solving these difficulties, the Dawes Plan constitutes a beginning—a beginning which may be imperfect, but which is a good beginning and whose final result will be the better in proportion as all those called to carry out the Plan act reasonably and cautiously. If, from among them, I select one as typical of the best, I am sure of the approval of all of you and of your not regarding it as a slur of any kind upon the rest but as an honor for all collaborators. This typical representative is the man of noble mind sitting to my left. I raise my glass and drink this good German wine to the success of the new spirit, which we all hope to follow, since it will lead us to peace and friendship—the new spirit embodied in Owen Young.

Such was the spirit in which Germany took up the work prescribed by the Dawes Plan. In the past three years, she has carried on the work loyally and she will, I am firmly convinced, continue to do so in the future.

LECTURE III

FINANCIAL POLICY AND RECOVERY IN PRESENT-DAY GERMANY

ONE of the fundamentals of the stabilization of the mark—and without its establishment, on a firm basis, the laboriously constructed system of the currency would have collapsed—was the balancing of the budget of the Reich. In my first lecture, I explained how the Reich had become more and more indebted to the Reichsbank through the discounting of Treasury bills during the course of the War and during the post-war period. A similar unsound policy was carried out, though not to such a degree, by the States and municipalities.

This entire financing was not, as was believed in foreign countries (particularly in France) during more than one stage of currency depreciation, maliciously and consciously carried out for the purpose of destroying the purchasing power of the mark and of ruining German capacity to pay reparations; on the contrary, the successive Governments of the Reich always endeavored, though with inadequate means, to regulate the budget and to support the mark in foreign financial centers. One who has carefully followed the political situation in Germany during the years 1922-1923 must recognize that the various Governments of the Reich at all times followed a policy of maintaining the currency, because, if for no other reason, the depreciation of the mark created the greatest difficulties at home. These diffi-

culties finally reached revolutionary proportions. On the other hand, each time the exchange rate for the mark became firmer, the result was an extraordinary advantage for the Government in the eyes of the German people and a strengthening of its position.

The fact that certain groups of German speculators and whole economic groups—particularly new commercial firms, which had risen during the inflation period, some of which, fortunately for Germany, later disappeared without a trace—were interested in the fall of the mark and contributed to it by their activities, can and should not be denied, but that any German Government facilitated or even brought about the fall of the mark is an invention entirely refuted by the facts.

It is true that the Reichsbank, during the management of President Havenstein, who died at the end of 1923, and the Government of the Reich lacked the necessary energy to refrain at the proper time from the convenient method of creating money by means of the printing press. Thus it occurred that in the year 1923, in spite of the extraordinarily high tax rates prevailing at that time, the needs of public financing were met only to a small degree by taxes and assessments; by far the leading source of income was supplied by the printing press (in the last months more than 90 per cent), so that at the establishment of the Rentenmark, the Government finally owed the Reichsbank the fabulous amount of 189.8 quintillion marks. In order to make clear the fantastic absurdity of this inflation figure, I should like to point out that, were I to write the amount according to the decimal system, I would have to attach eighteen zeros to the 189. To make a comparison,

were one to take old German thousand mark bills and put one upon the other, pressing them tightly together, one would have a pillar of such inconceivable height, as to be twenty-five billion times the highest mountain on earth. I cite this example, in order to show to what absurd heights inflation had reached in Germany when the Government decided to put an end to it at one stroke, by stopping the printing of bank notes and by balancing the budget of the Reich.

How was the German Government to survive the transition period, without the possibility of a foreign loan, until the new taxes fixed in gold were received by the Treasury of the Reich?

Here also the ingenious construction of the Rentenmark helped. There was created out of nothing, not only a currency, which was kept stable by the confidence of the people, but in addition a loan to the Government of nine hundred million stable Rentenmarks was effected, the Rentenbank placing at the disposal of the Treasury of the Reich nine hundred million marks of its certificates.

The Minister of Finance, Dr. Luther, who was at that time controlling the financial fate of Germany with a firm hand, believed that he would be able to get along with this amount until the beginning of January. Very soon, however, it appeared that this would be impossible and that the Reich would have to apply for an additional credit at the Rentenbank. This occurred during the middle of December. On December 20, however, the Board of Directors of the Rentenbank rejected the application of the Minister of Finance of the Reich. This was a decisive step toward recovery. If the Rentenbank had yielded,

there would have been grave risk that the Rentenbank would soon have found itself in the predicament of the Reichsbank and the people would have lost confidence in the Rentenmark.

A man of a different sort from Luther would have despaired, after this refusal, of the possibility of keeping the government financial machinery in operation and would have left matters to take their own course. Luther's energy, however, was doubled by the compulsion to strengthen the budget through his own power. Expenses were again reduced to the utmost, and the maturity of taxes was fixed at an earlier date than originally established by the so-called Emergency Ordinance. In this way the Reich managed to pass a critical period successfully and to enter upon a new year.

And now the various measures which Luther had taken for the purpose of stabilizing the budget gradually began to show results. The German Parliament had given the Government dictatorial powers to this end. By the so-called "Authorization Law" of October 13, the Government, that is, virtually the financial dictator, Dr. Luther, had been given the power to take all measures which appeared necessary for stabilizing the currency and balancing the budget.

When this authorization later became void through the fall of the Stresemann Cabinet on November 23, the new Marx Cabinet, in which Luther was again Minister of Finance, secured a new authorization law, after President Ebert, in the period of the greatest need, had issued the so-called first Emergency Tax Ordinance, pursuant to the so-called Dictatorship Paragraph in the Constitution of the Ger-

man Reich (Article 48), which is applicable only if the Reich is threatened with immediate danger.

Furthermore, Luther, as a result of the two authorization laws, now had the free possibility of energetically attacking the two great problems of limitation of expenditures and increase of revenue, for the purpose of balancing the budget. The restriction of expenditures was put through in the most rigorous manner possible and, as a matter of fact, for the purpose of saving the currency and the nation it was necessary to make such sharp inroads into the rights granted under the Constitution, that it is hoped there will never be a recurrence of this in German history. Those who suffered particularly from this were the Germans abroad, those who were injured as the result of liquidation and those who were driven out of the territories lost as the result of the Peace of Versailles.

Had their claims, which amounted to at least ten billion gold marks, been considered to their full extent, the balancing of the budget would have been impossible. It was therefore decided to settle at one stroke the claims of these unfortunates at a nominal percentage. It goes without saying that this was only an emergency solution and it became a matter of honor for the German Reich and for the German people gradually to satisfy these claims. This is why the present Government of the Reich is making an effort (which, in my personal opinion, is still inadequate) gradually to dispose of this question.

Furthermore, Luther had to reject the numerous claims still arising at that time from supplies to the Reich during the war period and deliveries, made pursuant to private agreements with foreign claim-

ants to reparations. Here also the Gordian knot was cut in respect to many claims, partly contested in lawsuits, by means of an ordinance having power of law, the so-called "Compensation Ordinance," the significance of which lay in the feature that all these indemnities were fixed in expedited proceedings and were paid by the Government at relatively low rates.

Luther once said later on, that all these devices could only be designated honestly as a partial bankruptcy of the Reich, but that without this partial bankruptcy, stabilization would have been impossible. Just as severe were the ordinances by which the rights of officials who had been appointed in the service of Germany for their entire lifetime, were attacked. This action was necessary because during the course of the War and the after-war period, a great inflation had occurred in the number of persons employed as officials, clerks, and workmen in public enterprises; in the administration of the Reich, alone, including the post office and railway, there were discharged, pursuant to the so-called "Personnel Retrenchment Ordinance" during the course of three months, one hundred and fourteen thousand officials, thirty-two thousand employees, and one hundred and eighty-four thousand workmen, whereby, despite the exceedingly low salaries paid to officials at that time, there was saved in expenditures for personnel alone, about three hundred millions yearly in gold.

To the same extent, the States, the provinces, and the municipalities were compelled to reduce their staffs of officials, so that about seven hundred and fifty thousand people were affected by this severe ordinance. The misery and bitterness created by this

action in Germany may well be left to the imagination.

Finally I wish to mention a last measure of economy, particularly inclusive in its action, which also signified a partial bankruptcy. The Government decreed by an ordinance with the power of law that public loans were not to bear interest or be paid off until the settlement of the German reparations obligations. This decree was an absolute necessity, for public debts at that time amounted to more than one hundred billion marks in Germany, so that there would have been needed for interest payments thereon annually, without sinking fund payments, five billions, which it would have been impossible to raise, and theoretically could not have been raised even by tripling the income tax. In this matter the Government frankly took the position that old loans—exactly like the bank notes of the Reich—had become worthless through the depreciation of money, as Germany had emerged from the inflation period with an exchange rate of a billion paper marks to one Rentenmark. This attitude, which originally might have appeared practicable, had to be given up later, owing to the pressure of the popular vote, particularly as the Government had fixed, in the same emergency ordinance by which it had discontinued the payment of interest on loans, a revaluation of mortgages at 15 per cent of their peace-time value. This was the point which enabled adherents of the German Revaluation Policy to take action to bring this question up again. Since then, the problem of revaluation, particularly the revaluation of public loans, of credit balances in savings banks, and of mortgages, has dominated the public mind in Ger-

many, and under the pressure of public opinion, which created a new party at the last elections for State and municipal representatives, namely, the Revaluation Party, the Government had to give way to a large extent.

In the year 1925 public loans, insofar as they were in the possession of creditors before a certain date,—so-called “Old Loans,”—were revalued at 12½ per cent. These old loans, however, do not for the time being bear interest, but are to be redeemed in thirty equal installments, in which connection there is paid back each time 4½ per cent interest with the redeemed amount. The defect of this manner of settlement is that the creditors cannot count on a definite income, but enjoy no more than the possibility of a lottery prize. On the other hand, the Reich, particularly in the severe years of reparation obligations and the payment of war pensions, must figure on a very considerable annual burden, which must be covered by funds produced by taxes. I therefore believe that a change must be made in this respect, such as I personally prepared as Minister of Finance of the Reich, a change from the unsound and unfortunate idea of a lottery prize to a fixed current interest rate.

This settlement is possible without the necessity of increasing the amounts which the Reich will require for its old loans during the next thirty years; redemption, of course, is left for a later period. Therefore, after it has once been carried out, it will in no way be detrimental to the finances of the Reich, and on the other hand will offer certain advantages to the owners of the bonds.

In general I am firmly convinced that no German

Government can at any time in the future admit a subsequent change in the settlement of obligations contracted under private law, on which the entire economic life is dependent, for the reason that, in my opinion, our entire economic structure would be severely shaken thereby. The two German Governments of the year 1926 have therefore, in order to prevent severe injury to the economic life of the German people, refused to comply with the demand for any other form of settlement of private claims dating back before the time of the inflation, and I believe that no German Government will ever adopt another viewpoint so that from this quarter any unbalancing of our economic life appears to be excluded.

I desire now to refer once more to the steps taken by Luther in the spring of 1924. I have referred to the ordinances by means of which he restricted the expenditures of the Reich but now I want to take up his tax laws.

The most important provision was that the collection of the taxes in gold currency, which had already been started, was now carried out universally and in this manner the public treasuries finally came again into possession of money which was not, as a result of depreciation, deprived of the greater part of its value on the long road from the taxpayer to the recipient of the salary. At the same time, however, the tax assessment rates were increased to an extraordinary extent; thus for instance the turnover tax was increased to 2½ per cent. Inasmuch as in Germany the turnover tax is not collected on the finished product but on every transfer of raw material, of the semi-finished product or of the finished product

from one hand to the other, one can easily imagine the effect of such a turnover tax of $2\frac{1}{2}$ per cent. As was soon proven by actual facts, it was an absolutely impossible tax and led to economic injury which simply could not be offset. Besides the turnover tax there were assessed very high property and income taxes in which connection the income tax, for the reason that for the time being there were no incomes in stable currency in Germany, or at least only in very rare cases, was an income tax in name only while in reality it also was collected on the basis of certain percentage ratios of the property or of the turnover.

In addition to these Federal taxes there were applied over a large part of Germany the so-called realty taxes which were collected by the States and by the municipalities; particularly the land tax and trade tax. As it was clear that in spite of this there would still be an enormous deficit, an entirely new kind of tax was introduced, namely, a tax on all rented houses, factories, and agricultural buildings, the so-called "house rent tax." Luther, in making this "invention" which made him many enemies in Germany, proceeded from the viewpoint that the owners of buildings, generally speaking, had not only saved their capital, but furthermore, by a repayment of mortgages in depreciated currency, had obtained a considerable reduction of their debts.

From this he deduced the claim of the public authorities to levy not only the realty tax but a special tax as well.

This tax has undergone continuous development in Germany. It amounts to as much as 50 per cent of the pre-war income tax and is one of the most productive taxes in the entire German tax system. The

total amount collected by means of it is about four times as high as the property tax and approximately as high as the income tax, *i.e.*, about two billion gold marks per year.

All these taxes, in order to eliminate the ebb in the public treasuries, were made payable immediately or within a short period of time and were collected with the greatest rigor. They were taxes of really brutal harshness in connection with which the Minister of Finance himself realized that they were not paid out of revenues, *i.e.*, from the profits of economic activities, but were rather taken from the very intrinsic value of the property itself. To this must be added that the Reich, States, provinces, and municipalities collected their taxes separately and that none of the public tax creditors showed any consideration for each other. In this manner the various public authorities in Germany, forced by the necessity of filling their empty treasuries, fell with all force upon the unhappy citizen who was on the verge of becoming crushed economically by this manifold taxation, the more so because, as I have already set forth in my first lecture, the entire economic life was depleted of any operating means and as credits could only be obtained with the greatest difficulty and at extremely high rates.

There cannot be any doubt that the tax laws of that time and the harshness in collecting the taxes were necessary. Luther himself some time later expressed this idea when he stated that the bitter medicine of restricting expenditures and increasing revenues was as necessary for the recovery of the German people as the good-tasting beverage of the Rentenmark. The German Government prescribed

both medicines to the German people as a part of the same treatment for the overcoming of the inflation fever. However, it was soon found out, using the simile of Luther, that the dose of the medicine given by the new tax law to the German people was somewhat too strong; the aim had been overreached. As was finally discovered, German economic life had been subjected to unnecessarily strong bleeding while at the same time the quantity of real blood, namely, the actual capital available, for economic life, had been overestimated.

Luther himself, who had a good conception of what was economically possible and necessary, started to reduce the taxes in the fall of 1924; however, these endeavors were strongly opposed by the entire German tax-collecting bureaucracy, especially by the Tax Administration of the States and municipalities; I still remember very well the conference of the Ministers of Finance of the German States held in the fall of 1925 to whom Dr. Luther explained his plans for the reduction of the government expenditures and of the tax burdens, when I, as Minister of Finance of Saxony, was practically the only one who was willing to accept his ideas. Soon after the new election of the Reichstag, Luther became German Chancellor; the lowering of taxes which was possible from the viewpoint of government finances and absolutely necessary from the viewpoint of German economic life, was started hesitatingly and was not carried out in an entirely successful and happy manner on account of having become the chief object of political compromises. On account of this the German tax assessment and the German tax collection in the years 1924-1925 contributed to

the credit emergency in economic life and in this way to the very difficult situation prevailing in the winter of 1925-1926 when the number of unemployed receiving doles exceeded two millions.

Thus the second Luther Cabinet which was formed in January, 1926, and to which I was called by the Chancellor as Minister of Finance of the Reich, was confronted with an entirely new situation. Whereas up to this time all forces had to have for their aim the maintenance of the currency, now—when the stability of the mark was beyond doubt while the future of German economic life was seriously endangered—all energies had to be concentrated upon the overcoming of the economic crisis. When I took over my office as German Minister of Finance in February, 1926, I was confronted with the following situation. On the one hand conditions in economic life had become hopeless; two million unemployed receiving doles spoke a warning in clear language as did also the number of the daily bankruptcies and business receiverships which reached record figures. I myself am an outspoken opponent of any government measures of assistance in economic life for the reason that I am convinced that economic life can only help itself out of its own resources and that any form of government subvention will sooner or later react upon itself. This principle of mine could not, however, prevent me, in view of the fact that the economic crisis in Germany was becoming more and more acute, from examining into the question to what extent government measures, especially in the financial field, had proven to be a disturbing factor in the complicated mechanism of economic life. On the basis of the statistical data available to me, I

came to the conclusion that we in Germany, in order to maintain our currency, had far overreached our aim in the assessment and collection of taxes and that a lowering of the tax rate was an absolute necessity in order to be able to keep our economic life in operation and in order to prevent a further increase in the number of unemployed. It is very difficult to say how many taxes were overcollected in Germany during the years 1924-1925; I myself am of the opinion that an amount of 1,500,000,000 to 2,000,000,000 marks is not too high.

What became of this money? The answer to this question led me to some very interesting conclusions which I am convinced are typical in the field of taxation and which are the same for all countries where similar phenomena may be noticed.

I believe that the following principle can be laid down for the administration of taxes and finances in all countries:

No condition is more dangerous, not only for economic life but also for public finances in general, than the collection of excessive taxes for, as a result, public authorities have too large means available; such excesses of public funds lead to a policy of extravagant expenditures which bears no relationship to the poverty of a people suffering from excessive tax burdens, and further involves the danger that the accumulating funds may be improperly administered by the public authorities.

We in Germany could note these two injurious consequences very clearly in the year 1926; the municipalities in particular failed to be governed by such a rigorous policy of thrift as was required by the poverty of the German people.

To this was to be added that all the public administrations showed a very strong inclination to use their large treasury holdings in order to expand; they bought real property, participated also in industrial enterprises of every description, organized banks and did a loan business frequently of a rather doubtful nature through such banks.

An especially dangerous chapter was constituted by the mischievous feature of granting government loans or subventions to needy private enterprises. It struck me as a particularly glaring example of such a senseless condition when a German contractor who conducted his business in a saving and economic manner had to see his taxes, the burden of which nearly broke him, used to assist his competitor, who was a less efficient worker, by means of government loans. In contrast to the full public treasuries, the disadvantages of which I have already described briefly in an example, the German people were struggling through a very severe crisis deprived of all operating capital, and although the extermination of German firms in such large numbers for the time being had brought about a selection of sound firms and a weeding out of many unfit economic structures dating from the time of the inflation, the conditions nevertheless had become so acute that they threatened to drag down the healthy ones into the abyss together with the diseased.

Confronted with this state of affairs, the decision to be rendered by the Government was self-evident. I considered it my most urgent duty to relieve the tax burdens immediately in order to be able to carry on a sensible and thrifty economic activity in the Reich, in the States, and in the municipalities on the

basis of our lowered incomes and our poverty. With this in view, a few days after I had entered my office I proposed to the Parliament a reduction of the tax burdens by about one-half billion gold marks and after very severe parliamentary struggles, the main tendency of which was to find out what taxes were to be reduced, the bill of the Government was passed by the Reichstag in a somewhat modified form. The Agent General, S. Parker Gilbert, remarked upon this reduction of taxes in his report of November 30, 1926:

The Reichstag has passed a program submitted by the Minister of Finance of the Reich for the purpose of relieving production and trade from some of the most crushing taxes and in order to bring the most important public expenditures in a general way more in proportion to public revenues.

At another place in his report he continued:

The budget situation is still healthy and the new tax program proves increasingly productive.

With these comments and with the establishment of this fact, S. Parker Gilbert, in the exact, clear, and very logical manner which all his reports show, touches the very point which I wanted to bring out in my program for a reduction of the German taxes.

I was, and I am, convinced that a financial policy which is intended to be lastingly successful must never be based on a fiscal or tax collection point of view but on an economic point of view only. The high taxes, especially taxes increasing the cost of production and therefore detrimental to economic activities, as, for instance, the German turnover tax, it is

true may bring about a financial salvation in case of most extreme need; in the long run, however, such taxes cannot be borne by any people who are a part of international economic life and dependent upon it.

To this is to be added that I was confronted in part by taxes which were directly prohibitive, as, for example, the Stock Exchange turnover tax which, when compared with the rate prevailing before the War and also when compared with the assessment rates prevailing on international stock exchanges, was so absurdly high that the business of the exchanges almost came to a standstill. I recognize, of course, that this is to be explained in part by the prevailing hard times. In this connection I reduced the rates to less than one-half and, as I had expected, success followed; on account of the increase in business, after the reduction of the taxes, the net tax revenue was considerably higher than previously. I mention this as an example of the difference between a tax policy based on fiscal and one based on economic grounds. I am convinced that any tax, in case it exceeds a certain percentage (which of course differs in accordance with the kind of tax concerned), is not only directly injurious to trade and industry, but also detrimental to government finances, inasmuch as it is only logical that the actual revenues must drop if a certain maximum assessment rate has been exceeded.

The entire aim of my tax reduction was therefore to maintain the tax assessment rates in such a manner that business was stimulated and that at the same time the revenues of the Government were increased. It must be understood that this could take

place only after a certain transition period, during which the consequences of the reduction had to express themselves. This experiment which, as is admitted now, was absolutely successful, was a very bold one and brought upon me many severe reproaches. I was called a frivolous young man, because the conditions prevailing in our economic life were so bad that for the time being the tax revenues dropped considerably. For this reason a step had to be taken which in my opinion was an absolute necessity for Germany, the separation of the regular from the special budget. A rich people like the American people can afford to cover the entire expenditures of a country during normal times out of taxes; a poor people like the German people who, after the last War, had to bear extraordinarily severe burdens as a result of the War (I need refer only to the reparations and the war pensions) in my opinion must take care that those government expenditures of which only later generations will reap the benefit (I have in mind such things as the investment of capital for the Post Office Department or for canal construction, profitable and necessary from an economic viewpoint) are not paid out of tax collections obtained from already overburdened business. Such expenditures ought to be covered by loans in the repayment of which later generations assist.

I admit that this form of financing of the so-called special budget may give rise to doubts (S. Parker Gilbert underscored these doubts in his latest report very heavily), in case expenditures are undertaken which are avoidable and which are unjustified from an economic viewpoint; I admit also that there is a

great temptation for a government which wants to maintain itself in power and must, therefore, be popular, as also for a Parliament confronted with reelection, to misuse such a special budget; I believe, however, that so far as Germany is concerned, the principle is correct that permanent and revenue-yielding investments should not be procured from taxation but from loans, and that this principle is the only one which can make it possible to maintain the balance in the budget without bringing it about that the tax burdens become unbearable. A necessary proviso of this financial policy is of course that the Government obtain loans. In view of the slowness with which savings are accumulated in Germany, the very greatest restriction of the special budget for Germany is a self-evident policy. The rather discouraging result of the German Government loan offered in February, 1927, in Germany (the interest rate, it must be admitted, was much too low), makes it absolutely necessary to limit any expenditures which are to be covered by loans. For the principle of thrift is, in connection with the expansion of the German budget, a *conditio sine qua non* of a balanced budget.

You, in the United States, in spite of your riches, have set an example for the entire world of the way in which, by well-organized and logically executed action, unproductive government expenditures can be avoided. It will be the endeavor of any German Government to reduce in the same manner all expenditures to the lowest possible minimum. Of course, the fulfillment of our political, educational, and social tasks sets limits to such reductions. Opportunities for thrift in Germany lie (in spite of the

fact that in this field a great deal has been done during the last few years) in the most general introduction of efficiency (rationalization) in administration, for which purpose the joint coöperation of the Reich, of the States, and of the municipalities is required. As Minister of Finance of the Reich, I set an example and carried out the rather thankless task of reorganizing my Department in such a manner as to avoid and eliminate any unnecessary work. I succeeded in permanently eliminating a rather considerable percentage of officials required in the Central Administration. One should not, however, overestimate the possibilities of restricting government expenditures by such a reform of administrative methods inasmuch as Germany, up to the present time, has effected extensive economies in this field only to find that these expenditures, when compared with the entire budget of the Reich, play a comparatively small part. I consider it out of question to reduce the budget of the Reich by more than \$25,000,000 per year, even with the introduction of the greatest possible simplification of methods, although with the coöperation of the States and municipalities, the total savings possible in this connection may be considerable.

The reduction in taxes decided upon by the second Luther Cabinet as a result of an earnest endeavor to reduce expenditures as far as possible brought it about that the budget equilibrium was maintained. These methods of reduction were adopted in conjunction with other government regulations for the purpose of promoting the export business and bringing about greater activity in the building trade. They

helped German economic life to overcome the severe crisis of the year 1925 in a comparatively short time.

This rapid recovery was not only a result of a tax policy based upon economic principles, which left the available operating capital as far as possible to the use of the business community and in this way increased productivity and revenues instead of drawing this capital into the treasuries of the Reich, of the States, and of the municipalities, but above all it was the result of renewed confidence among business men who were so encouraged by these measures that business soon revived.

Personally, I believe that the imponderable factors, such as the disposition of the nation, are generally underestimated when judging economic situations. I am of the opinion also that in order to be economically successful, the knowledge, energy, and experience of a man thrown upon his own responsibility are more important factors than the possession of means of production and operating capital; and I believe that confidence in the future which inspires the will to work is the decisive factor for the entire economic life of a people, and, above all, for the rehabilitation of a defeated and impoverished nation.

In the year 1926, after the severe crisis of the immediate past, this German faith in the future of our economic life and in the future of our nation was reborn. This undoubtedly led to many exaggerations; an exaggerated optimism appeared everywhere and the difficulties which were still confronting Germany were not sufficiently appreciated either in Germany or abroad. I myself, who always demanded in public speeches that all possible power and energy should

be utilized for the overcoming of economic catastrophes and called attention again and again to the necessity for hard work, was reproached for being too optimistic about things.

I have too deep an insight into German financial and economic conditions not to see the great dangers which are in the way of an ultimate recovery of Germany. The destruction of our national wealth caused by the War and inflation is so tremendous that for the time being we are eliminated as a financial power in the world market, while so far as our domestic conditions are concerned we are thrown back to the status of the sixties of the last century. All the savings which we accumulated during the last half-century of German economic prosperity have been entirely used up. To this must be added that in our weakened and decimated state of national wealth we must bear the burdens of a lost War including reparations, on account of which the tax burdens are nearly unbearable and the obtaining of a surplus in our economic life toward the formation of new capital is made practically impossible. For these reasons alone, to which must be added also a number of other very important reasons, I am of the opinion that the road over which the German people must pass will be exceedingly difficult. It might well be compared with a tunnel rather than a road, a tunnel in which only very, very far away is there beckoning, a very faint glimmer of light. But in spite of all this I am convinced that the German people, after extreme difficulties, will be able to work their way out of this tunnel of distress and will find a path which will lead from darkness to light.

I firmly believe in Germany. In spite of all and

everything I believe in the future of my people, not because I am an optimist and do not see the difficulties, but rather because I know the German people and because I know that it is perhaps the greatest gift of the German nation that misfortune fails to break its strength. It seems to strengthen it. The German people has shown more than once through the hard work of its spiritual leaders and its laboring classes a power which will enable it now to rehabilitate devastated Germany as it did after the Thirty Years' War. Our material riches are gone, but the power and strength of German labor have not been destroyed. It is true that war, inflation, and revolution have temporarily weakened the German nation, but essentially and so far as its will is concerned, it has remained sound and this, our greatest asset, I am firmly convinced will reobtain for the new Germany, on its democratic foundation, its position in the economic life of the world. Only allow Germany to work and I am convinced that a new Germany, for the great majority of whose people democracy and freedom are causes sacred to the heart, will become an important link in the chain of those great nations who see the historical task of our century to assure the peace of the world and to increase the well-being of all nations.

LECTURE IV

PROSPERITY AND DEPRESSION IN GERMANY SINCE THE STABILIZATION OF THE MARK

IN my first lecture, I outlined the history of the German currency disruption down to the point at which, after the creation of the Rentenmark, the stabilization of the Reichsmark was effected on the basis of four thousand two hundred billion paper marks to the dollar.

I described how the "Miracle of the Rentenmark" was, at the outset, rendered possible by two circumstances. One was that the German people, in their revulsion from the tortures of inflation, grasped greedily at the new medium; the other was the general feeling that Germany would be totally ruined if the experiment failed, a feeling which evoked such a firm belief in the Rentenmark that its weak and economically unsound foundation failed to exert any appreciable influence. Thus a breathing space was gained, in which the extremely energetic measures of the Government were able to take effect.

Parallel with measures for balancing the budget the Reichsbank strove vigorously to restrict the circulation and, in particular, to call in the emergency money. This emergency money was a serious evil in the currency. It had come into use when the fall of the mark was so rapid that even the most strenuous efforts of the note presses of the Reichsbank were unable to keep pace with the demand. Not merely had the Federal States, the provinces, and the

communes, the government railways and the other public services printed such money, but private concerns had been doing the same thing to an enormous extent; so that this manufacture of emergency money had come to be employed as a very convenient means of obtaining credit and making gigantic inflation profits. The occupied territories, however, under the pressure of the Separatist menace and of the French policy of violence daily exhibited before the eyes of the people, had not the same faith in the Rentenmark as was shown by the unoccupied territory; consequently, they held tight to their stocks of foreign bills and bought new ones with their emergency money.

In this way, it came about that, while, in Berlin, the Reichsbank, under the severest difficulties, maintained the dollar at four thousand two hundred billion paper marks (or 4.2 Rentenmarks), the dollar exchange rate on the Cologne Bourse, and in the Rhineland generally, showed the following curve:

Nov. 13, 1923	. . . . .	3,900 billion marks
Nov. 14, 1923	. . . . .	6,850 billion marks
Nov. 15, 1923	. . . . .	5,800 billion marks
Nov. 16, 1923	. . . . .	6,500 billion marks
Nov. 17, 1923	. . . . .	6,700 billion marks
Nov. 19, 1923	. . . . .	9,850 billion marks
Nov. 20, 1923	. . . . .	11,700 billion marks
Nov. 22, 1923	. . . . .	10,200 billion marks
Nov. 23, 1923	. . . . .	10,500 billion marks
Nov. 24, 1923	. . . . .	10,250 billion marks
Nov. 26, 1923	. . . . .	11,000 billion marks

This meant that, on November 26, almost three times as much was paid in German paper currency

for the dollar in the Rhineland as was paid in Berlin, where, in consequence of this curve, the rate was only nominal and only about 1 per cent of the foreign bills applied for were allotted by the Central Institute.

It was clear that the stabilization must fail unless this fever of speculation could be stopped. This was effected by an order of the Reichsbank, issued on November 17, 1923, that, from November 22 onwards, no emergency money of any kind would be accepted in payment by the Bank and that, by November 26, all emergency money in the possession of the Bank must be redeemed.

As the Reichsbank granted no further credits in paper marks, the speculators were forced to sell their foreign exchange in order to meet their debts. From now onward, the rates for foreign exchange fell in the Rhineland almost as fast as they had risen. On the Cologne Bourse, the dollar quotation on December 10, 1923, was identical with that in Berlin; it had sunk to four thousand two hundred billion marks and remained at that figure.

As Dr. Schacht says in his book *Die Stabilisierung der Mark*, the speculators had experienced not an accidental but a systematically effected checkmate, which, for a time at any rate, rendered any repetition of their maneuvers impossible, since, in the same proportion in which they had been compelled to disgorge foreign bills, the stocks of the Reichsbank had been increased.

Altogether, as a result of the tussle with the *devisen* speculators, the Reichsbank augmented its stocks of foreign exchange by about \$50,000,000.

The process of purging the exchange market of its emergency money was now energetically prosecuted.

Whereas the amount of emergency money in circulation at the beginning of 1924 may be estimated at a minimum as the equivalent of \$150,000,000, it had been reduced to about \$25,000,000 by the middle of June and had completely disappeared by the end of October.

Meanwhile, in pursuance of the Dawes Plan, the Reichsbank had been reconstituted as a new German note-issuing bank; on October 11, 1924, the new Bank Act came into force.

The reconstituted Reichsbank received from the Government the right, for fifty years, to issue notes, the note-issuing privilege which still pertains to the four remaining private banks of issue playing no practical part. The notes have to be backed by gold or foreign exchange to the extent of 40 per cent, and of this backing 75 per cent at least must always be in gold; but the 12 per cent gold backing of the deposits originally required by the Experts' Plan had to be dropped as incompatible with German conditions.

The redeemability of the notes in gold prescribed in principle by Section 31 of the Bank Act has, for the present, been suspended; it can, however, be introduced at any time by a joint resolution of the Directorate and the General Council. I hope that uninterrupted economic and political development of Germany will make it possible, within the visible future, to do away with this last relic of the days of currency turmoil.

Considering the great influence exerted on the disruption of the currency by the granting of Reichsbank credits to the Government, it was only natural that, in order to secure the stabilized currency, the

possibility of the Reich securing credit from the Reichsbank should be carefully restricted. I shall not go into details on this point; I will merely say that all disturbance of the currency by government interference is thoroughly guarded against, since the maximum credit permitted to the Government is one hundred millions on open account, which must always be balanced on December 31, while, moreover, one hundred and thirty-five millions of the government debt of two hundred and thirty-five million gold marks owed to the Reichsbank at the time of reconstitution must be settled in fifteen annual installments, the balance of one hundred millions remaining for the period of the concession.

As, owing to these very rigorous stipulations, the Government, to meet its requirements, had no possible opportunity of issuing short-term bills discountable by the Bank it was forced to maintain a permanent cash reserve of some hundreds of millions, which had an extremely undesirable effect in various ways. Consequently, during my term of office as Minister of Finance, I carried through, with the unanimous approval of the General Council of the Reichsbank, an amendment of the Bank Act whereby the Reichsbank is enabled to discount Treasury bills of the Government to a total of four hundred million marks. In this way, both the Reich and the Reichsbank have acquired greater freedom of action, and the permanent maintenance of a working fund of about one hundred millions has become unnecessary.

Nevertheless, during the whole time that I was Minister, I made no use of the power to issue Treasury bills, nor has my successor done so.

The organization of the Reichsbank provided for in the fundamental features of the Dawes Plan and partly amended by the organized committee has, so far, worked excellently, and the coöperation of the German and the foreign members of the Council of the Reichsbank has proceeded without friction, especially as in Mr. Bruins, the Dutch member, the Reichsbank has been given an admirable commissioner.

But the road traversed in the reestablishment of the German currency was not an easy one. It consisted of three stages, namely, to November 20, 1923, when stabilization began, to April 7, 1924, with its provisional stabilization of the currency by the restriction of credit on the part of the Bank and to October 10, 1924, with the final stabilization on the basis of the eight hundred million gold marks from the Dawes Loan. They were difficult stages. All the way along, they were marked by the gravestones of big firms and small ones who had not been sufficiently robust to undergo the cure. It is with this momentous period that I desire to deal briefly.

Reminiscences of the inflation period are among the most terrible that we can recall. In those days, the majority of the people sank deeper and deeper into misery, while the inflation profiteers grew richer day by day and, by their extravagant living, in Germany and out of it, did untold injury to the German name and the German cause.

Naturally, the distress in Germany caused by the currency disruption hit those hardest who had to live on their annuities. Although the French plan of retiring at the age of fifty or earlier and living on the interest of one's savings has never been the

custom in Germany, and men of means have often continued to work beyond the age of seventy, nevertheless, there existed a large number of people, especially women, who lived on their means or whose standard of living depended upon the addition of small annuities to their earnings. Among such people the distress was greatest. There were literally a crowd of formerly well-to-do persons who had not saved a cent out of their possessions in marks. These people, whose purchases formerly exerted great influence on the home market, became a burden upon the public welfare services, but the State was so poor that all it could do was to save them from absolute starvation; for the rest, they were left to eke out a joyless life of extreme bitterness and despair.

The position of employees was a little better; they at any rate received their salaries and wages in paper money more or less proportionate in amount to its depreciation. This arrangement worked so long as depreciation proceeded at a moderate rate; but when, especially from the summer of 1920 onward, the mark sank so rapidly that the money received on Saturday had lost 50 per cent of its value by Monday, distress and despair made themselves felt in these circles of society, too. Albeit every housewife hastened to turn her husband's salary or wages into food—the amount was usually insufficient to permit of other purchases—the depreciation was fleeter of foot and reached the baker's or the butcher's shop before she could get there. Appalling scenes occurred when the clerk or the workman discovered that the double payment he had received was just enough to buy half a loaf of bread but no more; and

the revolutionary temper caused by such a situation came very near to precipitating a catastrophe in October, 1923.

On the other side stood the inflation profiteers. There could be no easier way of growing rich than that of buying commodities with borrowed money. Whoever had opportunities of obtaining credit, in particular whoever could discount three months' bills with the Reichsbank or any other bank, was able, by skilful manipulation of these opportunities, to accumulate enormous quantities of goods. That was the period in which the big combinations were formed in Germany—not such organic structures as, for instance, the German Steel Trust of 1919 to 1926, which controlled the production of the various works and rationalized things on a uniform plan, but heterogeneous combinations of factories of all kinds having no sort of connection, such as the Stinnes concern. That these formations carried within them the seeds of decay is obvious. Enterprises of this description, started during the inflation and wondered at, not only in Germany, but generally throughout Europe, have almost all disappeared; and inflation profits heaped up by obscure individuals have, with few exceptions, also vanished, their accumulators having been unable to stand the credit strain of stabilization.

But, in the year 1923, the contrast between riches and poverty, and especially the tactless and snobbish display of wealth on the part of the inflation *parvenus* seriously increased the social tension in Germany.

Outwardly the manufacturing industry manifested a prosperity, not to say a boom, such as it had

never before experienced. The great regulator of all economic life, the law of supply and demand, seemed completely suspended. Every article produced was speedily bought up regardless of price because everyone in Germany knew only one quest, namely, the conversion of paper money into commodities. To these selling possibilities at home was added an unlimited possibility of sales abroad caused by the fact that German industry could work up material obtainable on the home market at a minimum, indeed scarcely more than nominal, cost. Most of the home raw materials bought with ninety-day bills cost scarcely anything, and the wages and salaries paid in paper marks equaled, expressed in gold, only a fraction of what the British and American manufacturer had to pay.

Hence, there were in Germany, at that time, hardly any unemployed. All factory chimneys were belching smoke, and every factory engaged as many hands as it could obtain or could find room for.

Today we know that this boom meant only pseudo-prosperity; the seemingly excellent appearance was, in reality, nothing but the hectic red on the cheeks of a fevered patient. Misled by our low costs of production, we were carrying on in Germany a dumping system of the worst character, which practically resolved itself into a national clearance sale and meant an enormous reduction of the national wealth. For not only were goods being dumped abroad; shares were being sold, and landed property, especially large town houses, were passing in considerable numbers into the hands of foreigners. Cases occurred of tenement houses with a peace-time value of \$100,000 being sold by their impoverished and distressed Ger-

man owners for a few thousand Swiss francs or Czech crowns; and though some of these properties thus sold for a mere song have since passed again into German hands at considerably enhanced prices, a large number of them still belong to foreigners.

Those were the days when one could travel first-class from Hamburg to Munich for a couple of dollars, the days in which Germany, in particular Berlin, was flooded with foreign buyers, who, with their tempting *devisen*, were able to buy up German wares at a slight fraction of their real value.

After the stabilization of the mark, the "pseudo-prosperity vanished like a puff of smoke. This was caused, in the first place, by the payment of wages and salaries in stable currency; and though, at first, these wages remained far below the pre-war level and below also the post-war level reached in other countries as a result of the general high prices, the days were over and gone in which wages formed an almost negligible factor in the calculation of costs. Moreover, it was obvious that raw materials had now to be bought at fairly normal figures and paid for in stable money; in addition, there was the credit difficulty which assumed really catastrophic dimensions and became the most menacing of all specters.

The credit stringency was so excessively severe because, with very few exceptions, German firms had lost their working capital.

True, well-managed concerns, whose heads had learned in good time to think in terms of gold-currency, had, to a fair extent, preserved their capital by investing it in premises, plant, and stock. But, in consequence of the *devisen* legislation necessary in Germany, they had no means whatever of main-

taining their working capital. The Dawes Plan was, therefore, quite right in stating that the machinery of German production was completely lacking in oil, that is, in working capital.

Thus, the deflation crisis set in in Germany with terrible effects. Regarded absolutely, the demands made upon the German money market were not so very great; but, owing to the utter deficiency of capital, they were incapable of being met, so that loan money acquired the value of a rarity, and obtained interest rates which, it is to be hoped, we shall never see again.

In November and December, 1923, interest rates of as much as 30 per cent per day were asked and paid; and juridical decisions were given in Germany to the effect that interest charges of up to 22 per cent per day, in November, 1923, were not regarded as *contra bonos mores* but as justified by the state of the money market. I personally know a case, in which a medium-sized German firm which had been debited for a few days with fifty thousand marks on account of some days' delay in the payment of certain foreign checks in December, 1923, was charged a like sum for interest at the end of the month.

Without doubt, the money lenders, above all the banks, recovered, by means of these high rates of interest, a portion of the losses experienced through paper mark credits, and were thus strengthened for their coming tasks. But the needs of industry and trade were increased to an incalculable degree by these interest rates and, as I shall show, by the rigorous collection of debts caused by a cruel tax policy.

No wonder that, in these circumstances, a severe strain was put upon the Reichsbank and that the preservation of the currency, which was still a very weak and frail plant, was severely jeopardized.

As the Reichsbank rightly saw its chief task in the preservation of currency stability, it proceeded, in April, 1924, to introduce the famous restriction of credit, which obtained for Dr. Schacht the nickname of Lord High Executioner of German economy.

That the form of this credit restriction was not altogether happy cannot be denied; nor can it be denied in the case of other acts of interference such as the equally unhappy, though morally justifiable, action of the Reichsbank President on the so-called Black Friday of May 13, 1923, which did great temporary damage to German economy. But, nevertheless, Schacht's energetic measures were justified later in the stability of the new German currency: by forcing industry to part with the foreign currency and bills held till then as reserves, these measures soon placed the Reichsbank in a position to return to normal market conditions as regards foreign bills instead of the allotment as had been the case for months—of about 1 per cent of the bills applied for, in order to maintain the dollar rate at par.

The success of the Reichsbank policy is to be seen in the fact that the total stocks of gold and foreign exchange held by the Bank rose from the four hundred millions to which it had shrunk by the beginning of the stabilization to:

592 millions on April	7,
977 millions on July	7, and
1,256 millions on August	7.

But this Reichsbank policy—admittedly and indisputably successful as it was in removing the German currency still further from the danger zone—had nevertheless the terrible concomitant effect of causing great havoc in the ranks of German business. This is most evident from the bankruptcy returns. In March, 1924, the filings were 68; in April, 133; in May, 322; in June, 579; in July, 1,173; while the businesses placed under receivership, though totaling only forty-three for the entire first quarter of 1924, reached eight hundred and forty-five in July alone.

Although a large number of these firms thus swept away were creations of the inflation period, so that their disappearance helped to reduce the greatly inflated apparatus of production and distribution in Germany to fairly normal dimensions, it cannot be denied that, in this summer of 1924, a whole series of sound and capable firms were ruined by lack of capital.

This clearly indicates that the mere possession of means of production, coupled with well-managed and energetic labor, is not sufficient to maintain the economy of a great people; there must be the assistance of a certain amount of capital. But the German money market had been almost completely destroyed by inflation. This is best revealed by an examination of the deposits of those German organizations which generally act as lenders in Germany.

For more than fifty years, the savings banks, managed mainly by the communal authorities, had been the institutes entrusted with the savings of the bulk of the German people. The savings in these banks had increased, by the end of 1913, to nineteen thou-

sand six hundred and eighty-nine million marks. The money had been absorbed chiefly by the mortgage market, but public loans had also found the savings banks ready and willing to take up issues. The savings were completely destroyed by inflation. Consequently, the savings banks played no part whatever as lenders of capital during the year 1924. True, exceedingly active saving commenced immediately after the stabilization of the currency; it was as though the whole population, so soon as the "Refuge in Commodities" was over, began to save money with redoubled ardor, everyone being impelled thereto by the very natural wish to reaccumulate as rapidly as possible his emergency and old-age reserve fund which the inflation had swallowed up. Accordingly the deposits in the savings banks accumulated with extraordinary speed—faster, indeed, than ever they had done in pre-war years. Whereas, by the end of 1924, the deposits aggregated only fifty millions, they had reached, by the end of 1925, 1.6 billions; by the end of 1926, 3.1 billions; and, by the end of 1927, had passed the four billion limit.

The movement still continues. It is clear evidence of the German people's determination not to go under. It is clear evidence, too, of their restored confidence in the stability of the new currency. It is also evidence of a remarkable thrift, since the wages of the people are relatively small, the taxation burden is heavy and the cost of living high; and yet the people pinch to save a few marks every month. The monthly increase in total savings in Germany amounted, in 1926, to 121.8 million marks; it will probably reach an average of one hundred and fifty million marks for the year 1927.

Nevertheless, it will be a long time before the deposits in the savings banks become effective on the money market, especially since enormous sums are absorbed by mortgages for the building of new houses to meet the housing shortage.

Just as the inflation wiped out the deposits of the savings banks, so, too, did it wipe out the funds of the insurance companies and coöperative societies, amounting in 1913 to more than ten billions. Here, again, albeit in more modest proportions, fresh capital has been accumulated. If the curve continues as at present, this capital will, however, not make itself appreciably felt for some years.

Coming to the banks proper, whose pre-war funds were far below those of the savings banks, it is to be noted that they saved a rather larger share of their capital, though the loss here, also, was so great that, as against capital and deposits aggregating fourteen billions in 1913, they held only three billions at the end of 1923.

Since then, the total credits (chiefly short-term and long-term deposits) in the six largest German banks have developed with great rapidity, namely, from 1.06 billions on January 1, 1924, to 6.5 billions on April 30, 1927.

Then there are the public banks, *i.e.*, the State banks of the various Federal States and the communal banks and savings banks focused in the central clearing associations. These played a relatively big part as lenders of capital, especially in 1924 and 1925, the reason being that in those years, these banks had at their disposal a large share of the proceeds of a too rigorous tax policy.

Since the taxes in Germany have been reduced to

the proportions necessary for State requirements, these public banks have lost much of their dominating character. Personally, I consider it a welcome symptom of gradual recovery in economic matters that the old pre-war relations of our private banks to our public banks are gradually being restored.

We shall have to pay the very greatest care in Germany to the restoration of our money market; we shall need whole decades of redoubled effort and economy to regain what was lost through the War and the period of inflation. Considering the pertinacity of the German people, particularly in the matter of saving, I entertain not the slightest doubt that this restoration of our money market will be carried through; but it will be accomplished slowly. In the meantime we can maintain our high level of production only, if, to use the phraseology of the Dawes Plan, our productive machine is lubricated by means of foreign credits.

Hence the foreign credits constitute one of the most vital questions in Germany. Considering the importance of the subject and the interest which, I believe, America takes in the question, I shall deal with it in detail later.

The adoption of the Dawes Plan having rendered it possible for international finance to recommence the regular granting of credits to Germany, foreign capital has begun to flow into the country, the deflation crisis has been successfully dealt with, and the position of German economy has gradually improved.

The numbers of unemployed, returned as one million five hundred and thirty-three thousand on January 1, 1924, fell to five hundred and thirteen thou-

sand three hundred and sixty-five by October 1, 1924. At the same time the bankruptcy and receivership filings also diminished in number, and a certain tranquillization became observable in business life.

But, as early as the summer of 1925, indications of a fresh crisis became apparent. The Stinnes crash was only an outward sign of the high tension obtaining in the economic atmosphere of Germany at that time. By the autumn of 1925, it had become clear that the previous recovery was only a short intermezzo. In the following winter, the economic curve experienced a sharp drop, and unemployment in February, 1926, reached the startling figure of over two millions—a figure at once indicative of intense social misery and a warning of political danger.

What is the explanation of this new economic reverse? Were we faced merely with a phenomenon which, in the continued abnormal situation, had hit economy with augmented force, or had we to look deeper for the causes?

The latter was the case. We found ourselves, not in a normal crisis, but in a situation due to special factors coming partly from beyond the German frontiers, partly from within.

Two of the external factors may well be stressed—factors of especial moment, inasmuch as they seriously affected the very basis of German heavy industry, namely, the coal and iron trades.

As regards the iron industry, the collapse of the French franc was of decisive moment. Germany was now passing through what the other countries had experienced when the depreciation of German currency led to the dumping of German products.

The fall of the French franc and the consequent

low costs of production obtaining in France made it impossible for German iron and steel to compete on the world market. Whereas, in pre-war Germany, the average monthly output of pig-iron had been 1.6 million tons in 1913, the monthly average in 1925 was only eight hundred and forty thousand tons, and fell to its lowest level of six hundred and thirty-one thousand tons in February, 1926.

The hopeless condition of the coal industry was due to external causes also, the chief of which was the subvention policy of the British Government in the year 1925, which rendered the situation very difficult for non-subsidized German coal.

Altogether, the position of the coal trade had greatly deteriorated owing to the natural developments of recent decades; and I am personally convinced that this deterioration will continue, that it will, indeed, become acute unless the liquefaction of coal or some other technical exploitation of it neutralizes the effect of this natural development.

The world's output of coal still lags behind the one thousand two hundred and seventeen million tons mined in 1913; it aggregated, in the year 1926, only one thousand one hundred and eighty-four millions. But the output in Europe has fallen off to a much greater extent. Whereas, it totaled, in 1913, six hundred and seven million tons, only four hundred and fifty-nine million tons was mined in 1926, a fact which can only in small part be attributed to the British coal strike. In reality, deeper reasons exist for the restricted production; the explanation lies in the continually falling demand; in Europe, at any rate, coal is being ousted more and more from its dominating position.

One reason for this is the increased use of lignite, which can be mined far more easily and is, notwithstanding its lower caloric value, cheaper than coal when it can be used on the spot for such purposes as the production of electricity. This fact has led to a rapid development of industries in central Germany, based upon the use of lignite. In these extensive lignite districts, gigantic electricity works have been erected and plants—such as the Leuna Works near Merseburg—have been established by the chemical industry. But, in Europe, coal has also to meet severe competition in the shape of the so-called “white coal,” the electric current produced by water power. Owing to its mountainous character, Europe has a relatively large amount of economically exploitable water power at its disposal, so that, at no very distant date, all her railway trains will be run electrically, and the railroads, which, hitherto, have been such big buyers of coal, will practically cease to purchase it. It is scarcely necessary to mention that such modern means of transport as the motor-car and the aeroplane are independent of coal. It remains to be seen whether, by the extraction of the requisite fuel out of coal-derivatives, a change in favor of coal may come about. At present, in any case, the use of kerosene and gasoline has cut coal off from an important direct market.

Finally the improvement in heating methods is no inconsiderable factor. Owing to technical progress, the amount of coal required to produce a given quantity of steam has been reduced by 40 per cent; and, though insufficiency of capital has retarded the change to modern heating plants in Germany, this conversion will unquestionably have to be carried

through very shortly, and the coal trade will thereby suffer further detriment.

It is no wonder that, under these circumstances, the coal industry entered upon a critical stage after the resumption of full working on the part of the coal mines which had been in part destroyed and in part injured by extravagant mining. The production being far in excess of the demand, prices dropped severely and many mines were unable to produce coal save at a loss.

In normal times the situation would have righted itself, inasmuch as the unprofitably worked mines would have disappeared and the lower price at which the well-conducted undertakings were able to supply coal would have led to an increase in consumption and demand. Instead of this, we received a sad proof of the extent to which the War and its consequences have blurred our economic reasoning and had resuscitated long-dead notions of protectionism and mercantilism: instead of leaving things to find their natural level, the British Government decided to subsidize coal and thereby made confusion worse confounded. I mention this fact expressly for the following reason, namely: it appears to me particularly typical of the confusion of economic ideas in post-war Europe, that the Government of such a far-sighted and economically inclined people as the British should have adopted a policy which, as the British coal strike later demonstrated, was very difficult to reverse.

The German coal industry suffered excessively in consequence of the British subsidies and the dumping of British coal. In 1913, the monthly average output in the Germany of that day totaled 15.8 mil-

lion tons and, as defined by present frontiers, 11.7 million tons; whereas, by the time the British subsidies ceased in April, 1926, the total monthly average in Germany had sunk to ten million tons. The number of workmen employed in the Ruhr Basin declined from four hundred and twenty-six thousand in 1913 to three hundred and sixty thousand in 1926, and even these could not be given full-time employment.

Naturally, the difficult situation in basic industries soon affected derivative industries; iron and steel products, especially machinery, suffered to such a degree that the position of these industries became distinctly critical.

In addition to all this, the situation of agricultural industry and of the building trades—in which home conditions, not international ones, were the decisive factors—exerted an unusually detrimental influence on the general economy of the country.

During the years leading up to the inflation crisis of 1923, German farmers had seen good times and inflation had eliminated the major part of their indebtedness; but, after the stabilization of the mark, they soon got deeply into debt once more. Long-term credits being unobtainable, they incurred short-term debts at exorbitant rates of interest, which, accustomed as German agriculture had always been to moderate interest, could not possibly be borne for any length of time. Moreover the necessity for meeting bills and other short-term debts forced the farmers to sell their produce at any price they could get; this led to figures for agricultural produce—in particular for Germany's important rye-crops—quite out of proportion to wage-rates and to the costs

of manufactured articles which the farmers had to purchase. The result was a sharp decline in the purchasing power of the farming population who were consequently obliged, not merely to curtail household consumption, but also to restrict their purchases of machinery and fertilizers, which, in its turn, greatly reduced agricultural productivity.

An old German saw runs: "*Hat der Bauer Geld, hat's die ganze Welt*," a saying which may be turned into English thus: "When the farmer has wealth, the whole world is in health." This is still true to-day; hence, despite the industrial development of Germany during recent decades, the purchasing capacity of her home market is still largely dependent upon the economic state of her agricultural classes, and the distress in the farming districts has accentuated the general fall in the demand for manufactured commodities.

In the building trades the situation was determined, as in other cases, by such State interference in economic matters as invariably leads to intolerable conditions. For social and political reasons, people had believed it necessary, during the period of inflation, to keep rents as low as possible; and, after the stabilization, it did not seem feasible to adjust rents to the general level of prices. Thus it came about that one could frequently occupy a large flat in Berlin for a few dollars a year, that is to say, if one had the good fortune to be the tenant of such a flat; while, on the other hand, the ridiculously low rents made the building of new dwellings absolutely impossible from the business point of view. Hence the unprecedented housing shortage which prevailed in Germany.

To meet the emergency, it was decided to build houses with public funds. This effort, however, proved a fiasco, as all attempts to preclude private initiative and to neutralize the price-regulating law of supply and demand by bureaucratic decrees are bound to do.

The housing shortage grew worse and worse. Moreover, the problem was not only a social but also an economic one. It was not merely that hundreds of thousands of unfortunate people—kept waiting for years on the official allotment lists—were obliged to put up with the most shocking housing conditions, but also that hundreds of thousands of building workers were kept unemployed, and, owing to the importance of the building trade as a key-industry, people in many other trades and callings were also thrown out of work.

It is by no means strange that such factors as all these, of which I have selected only a few examples, should have put a quick end to the brief revival of German economy after the end of inflation. The exceptionally difficult situation thus created was rendered all the more complicated as a result of the tax policy employed after the stabilization. The two years during which the taxes introduced in the autumn of 1924 were raised in Germany for the purpose of balancing the budget and of safeguarding the currency proved clearly that no nation participating in international economy can permanently endure such taxation without destroying its own economy and thus stopping its prosperity at the source. During the years 1924 and 1925, German economy in general—there were of course exceptional cases—was forced, not only to pay over to the

State its entire mobile capital, but, in addition, to borrow abroad, at intolerable rates, money wherewith to pay taxes. Hereby our costs of production were increased to such an extent as to affect severely our capacity to export and compete in the world's markets.

LECTURE V.

THE PROSPECTS OF THE DAWES PLAN

I HAVE in my previous lectures endeavored to give you a picture of the financial and economic situation in Germany in recent years. Today I am going to speak about the prospects of the Dawes Plan and to make some personal contributions to the discussion of this important question which is, in my opinion, of the greatest significance not only for Germany but for the entire world.

I have already shown how the European nations, after the War, found themselves with respect to the question of reparations lost in a dark jungle, from which no one was able to show a way out. But instead of bending all their energies toward finding a way out they started blaming each other for their plight and, like the heroes of the Iliad and of the Odyssey, they fought against each other great battles of words. The jungle did not shed its darkness as a result of this resort to big words and the confusion increased from day to day.

Through the great work of Charles G. Dawes the situation has been completely changed. It is significant that the change took place at the very moment when, in the place of force, a feeling of fairness arose and a sense of economic realities; light was shed suddenly upon the jungle and the way to the open for the straying nations of Europe became apparent.

What was the contribution of the 'Dawes Plan?

It was the idea, based on a deep knowledge of the foundations of the economic structure of the world and of international monetary relations, that upon Germany there could be imposed no more than an obligation to surrender in her own currency a certain sum of money to a trustee for the Allied and Associated Powers; that, on the other hand, the transfer of these mark sums to the individual countries outside of Germany was to be placed in the hands of a committee whose duty it was to undertake the transfer of these sums with due regard to the German monetary situation.

Germany's obligation is performed upon her delivery of the amount of her annuity as fixed by the Dawes Plan to the Agent General; all the rest, that is the transfer, no longer rests with her and is not under her control.

If we desire to gain a clear insight into the prospects and future possibilities of the Dawes Plan, we must separate these two points in our minds: (1) the raising of the annuities by Germany; (2) the transfer of this sum to the nations entitled to it. I shall deal first with the raising of the sum by Germany. How great is this sum? It varies in the first period up to the so-called standard year which begins on September 1, 1928. The experts started from the assumption that Germany would require some time to recover from the heavy losses of the War and of the inflation; consequently they established for Germany a respite of four years beginning on September 1, 1924, and ending on August 31, 1928. During the first year of this respite Germany was to pay out of her own funds but two hundred million gold marks, to which there were added eight

hundred million gold marks originating from the so-called Dawes Loan. For the second year the payment amounted to one thousand two hundred and twenty million gold marks. Toward meeting this payment Germany was afforded the possibility of selling preferred shares in the Federal Railways to the par value of five hundred million gold marks, so that the amount payable out of her own Treasury funds amounted to seven hundred and twenty million gold marks. In the third year one thousand two hundred million gold marks were to be paid; in the fourth year, which begins on September 1, 1927, the payment increases to one thousand seven hundred and fifty million gold marks, and thereafter amounts for the so-called standard year to two thousand five hundred million gold marks.

The figures are not unchangeable; the experts have given their plan a certain elasticity by making provision during the first four years for a contingent additional payment out of the actual proceeds of the so-called pledged revenues. This additional payment was not to exceed five hundred million gold marks and was to be paid in the fourth and fifth annuity years.

In my capacity as Minister of the Treasury I made an arrangement with S. Parker Gilbert to the effect that instead of the five hundred million payable in the fourth and fifth annuity years Germany was to make a single payment of three hundred million gold marks in the third annuity year. This arrangement offered to the Agent General this advantage, that during the third annuity year the resources available were increased by regular monthly payments and the sharp rise from one thousand two hundred

million in the third year to one thousand seven hundred and fifty million in the fourth year was in part avoided.

For Germany the advantage lay in the circumstance that instead of five hundred million gold marks we had to pay only three hundred million gold marks, which constitutes a very large discount or, one may even say, a certain abatement on our obligations.

For the first time an amendment of the Dawes Plan has been agreed upon between Germany and the Reparation Commission; the agreement was reached with a complete and unprejudiced understanding on the part of all concerned and has, I believe, afforded proof that the spirit that actuated the authors of the Dawes Plan, that is, the spirit of fairness and of realization of economic exigencies, is still living and controls the relations of the Agent General to the German Government. I believe that in the interest of the economic peace of the world everyone ought to desire this loyal coöperation to continue undisturbed.

Permit me to say here that the Agent General, S. Parker Gilbert, offers in my opinion the best guaranty of a proper and frictionless operation of the Dawes Plan. I shall refrain from giving a judgment on this highly gifted man with whom I have always worked most satisfactorily; but one thing I must say, and that is, that S. Parker Gilbert, however ably, wisely, and strenuously he upholds at all times the interests of the Allied and Associated Powers (I found this out more than once in the course of personal negotiations), has always acted toward Germany,—whose financial, economic, and political

situation he thoroughly knows,—loyally and fairly. I believe that I am not exaggerating in maintaining that America, who through the drawing up of the Dawes Plan has rendered a great service to Europe, has added a second and equally important service in sending over S. Parker Gilbert as Agent General.

This is important in its reaction on public opinion in Germany. I showed in my second lecture how energetically the adoption of the Dawes Plan was opposed in Germany by the extreme Left and by the extreme Right and what political difficulties arose from the adoption of the plan.

One of the main difficulties lay in the circumstance that in the Dawes Plan foreign commissioners were proposed for the Federal Bank, for the Federal Railways, for the pledged federal revenues and for the industrial bonds. Such devices had been resorted to in Europe only in the case of Turkey, and I believe that you will realize that the national pride of a people with a glorious past rose vehemently against the acceptance of such foreign commissioners. The reproach that is constantly leveled against us who have accepted the Dawes Plan and want it carried into effect is that we have surrendered a part of the sovereignty of our country. The wound still smarts and it is felt in Germany by everyone without exception. If this burning wound no longer so deeply poisons our domestic policies in Germany as it used to, this is due to the tact and consideration of the men who have undertaken the burdensome duty of exercising official functions in Germany and to the Agent General himself. This seems to me further proof that even the most difficult questions can be solved if good will and fairness exist on both sides.

I revert, however, to the payments that Germany is to make according to the Dawes Plan. I have already mentioned that during the respite they increase gradually to one thousand seven hundred and fifty million gold marks and in the standard year amount to two thousand five hundred million gold marks. This sum is made up of the following items:

Interest and amortization on the German	
Railway Bonds	660 million
Interest and amortization on the German	
Industrial Debentures	300 million
Transport tax	290 million
Budget	1,250 million

It seems to me very important to point out that in my opinion the enumeration of the various sources from which these payments are met is material only insofar as various revenues are set apart for the reparation service and are placed under the control of foreign commissioners.

As a matter of fact, it is of course a matter of indifference so far as Germany's economic structure and the German budget is concerned whether these sums are raised in the form of taxes or in the form of interest on industrial bonds or in the form of an increase of railway freights. In my opinion, therefore, when considering the German tax system it is always necessary to bear in mind that to our official taxes there are added these Dawes charges which are not covered directly by the budget.

How did the experts arrive at an assessment of two thousand five hundred million gold marks for the standard year? In the report of the experts we find no more than a clear and instructive exposition

of the factors that control Germany's ability to pay; how the experts arrived at this precise sum of two thousand five hundred million gold marks is not explained in detail. The fact is that this sum is merely an estimate; and it is known that until the very last days before the publication of the report the question of the amount of this sum was in dispute, the idea having prevailed at times that the standard payment should not be in excess of two billion.

The fixing of this amount could be an estimate only, for in the whole history of the world there is no case that might have served as a precedent. After the war of 1870-1871 France had to pay to victorious Germany four billion gold marks; that is, as far as I am aware, the greatest sum that a nation has ever had to pay to another in consequence of a war. Germany is now to pay according to the Dawes Plan for an indefinite number of years more than one-half of the amount that France was called upon to pay once. Furthermore it is to be pointed out that these four billions were the total war indemnity paid by France, while Germany through the delivery of the goods specially provided for in the Treaty of Versailles, in particular of ships, railroad material, cables, coal, chemical products, etc., has already paid on reparation account a sum which is estimated by Lujo Brentano at 41.6 billion and by the Institute of Economics of Washington at 25.8 billion. Taking as a basis the American estimate, Germany has already turned over to the Entente assets the interest on which at 5 per cent amounts to more than one-half of the standard payment under the Dawes Plan.

There is the further circumstance that through the Peace of Versailles Germany's capacity to pay

has been greatly impaired by territorial cessions, in particular by the loss of the Coal District of the Saar, of the Upper Silesian industrial region and of the commercial city of Danzig. To these losses there is to be added that the new boundaries of Germany are such as to cause heavy expenditures.

I shall refrain from going into details and I shall merely point out that although Germany has lost 20 per cent of her territory, she has a boundary ten thousand miles longer than before—mainly on account of the Polish corridor which tears Germany apart. You will easily realize that unproductive expenses are laid upon Germany by the necessity of guarding such a boundary for customs purposes.

Moreover, Germany's ability to pay was greatly impaired by the confiscation of German property abroad, a circumstance which weighs heavily in the balance both in connection with the raising of the reparation sums in Germany and their transfer abroad. I shall give an example. I estimate that the release of German property in the United States may well bring to the German Treasury an annual aggregate additional revenue of forty million gold marks by way of taxes of all kinds. From the standpoint of Germany's ability to meet reparation payments and of the proper operation of the Dawes Plan it is therefore of the greatest importance that the question of the release of German property be solved in the spirit that is actuating the American Government in this matter.

This is particularly important for the distant future. There is no doubt that Germany for the time being and in the near future will meet her obligations arising from the Dawes Plan. But will Ger-

many in the long run be in a position to raise the necessary sums?

The question must be considered from two different points of view: (1) from the point of view of the budget; and (2) from the point of view of the economic situation. As to the budget, the experts start from the assumption that Germany, owing to the collapse of her currency, has got rid of her internal debt and is therefore afforded the possibility of raising the necessary funds for reparation payments. Keynes, to whom we are indebted for many wise contributions upon the question of the German budget and of reparations, went further and remarked that, were it not for reparations, the Minister of the Treasury of the Reich would find himself in a sort of financial heaven. Unfortunately, upon my entering into office I had to tell him that, if I were to apply to my office any conception of the kind, it would appear to me more accurate, in view of war pensions, unemployment subsidies and reparations, to compare the entrance to my office room with the famous gate of Hell upon which Dante placed the words: "All hope abandon, ye who enter here."

Nevertheless, I acknowledge that the contention made in the experts' report that Germany was to devote to her internal debt as well as to her naval and army expenditure considerably smaller sums than other nations is from a budgetary point of view entirely correct. But from an economic point of view it makes a great difference whether the proceeds of taxes are used for military expenses, in which case the money expended remains in the country, creates employment for labor and capital and new sources

of taxation, or whether these proceeds are to be sent abroad.

The situation is the same in connection with interest upon loans. If the interest is paid in the country, it creates new taxable income, new purchasing power which stimulates economic activity, and insofar as it is saved, new capital which is available for investment, while the reparation sums are entirely lost to the country and to her economic organization. But here I am bordering on the question of transfer with which I shall deal in my last lecture.

Let me go back to the German budget. The balancing of the budget including reparations is so difficult because Germany in the next few decades will have to bear, in addition to reparations, her own war pensions, which in all the other countries that took part in the War are partly covered by the annual payments of Germany.

We are therefore compelled in Germany, in order to be able to shoulder the burden, to exercise the greatest restraint in all government expenses, which leads to certain consequences socially and politically objectionable. Permit me to give you an example of this curtailment of our expenses to the very minimum. A German veteran who is completely incapacitated (owing to the stringent medical examination but few are classed as completely incapacitated) draws a total annual pension of but \$330.

In spite of this curtailment of expenditure, the coincidence of payments for German war damages and German war pensions with reparation payments entails the necessity of an extraordinary tax burden in Germany. The experts' report states (and I personally agree thoroughly) that the burden rest-

ing upon the German taxpayer ought in justice to be commensurate with that borne by the Allied taxpayer. In their view, nothing but the most compelling and proved necessity should operate to make it lighter.

One of the most difficult questions of international comparison in the field of finance is to compare correctly the tax burden of different nations. Large books have been written on this subject and I feel convinced that many a young student may find here an interesting subject for his doctoral dissertation. However complicated this question may be in its details, one thing is beyond dispute, and this is that the tax burden of the German people as a whole is far greater than the burden of any other large nation.

To give you an example I may mention that we in Germany, in addition to the turnover tax with which taxpayers in America and Great Britain are fortunate enough to be unacquainted, have an income tax which hits one-third of our entire population (twenty-two million out of a total of sixty-three million), while in the United States out of a total population of more than one hundred and ten million, only five million are income tax payers. This is due to the fact that in Germany the income tax is assessable on as low a yearly income as \$280, so that every workingman is compelled to pay, while in America, according to the statistics I have before me, unmarried persons are exempted from income tax up to an income of \$1,500 and married persons up to an income of \$3,500.

Aside from the social and political difficulties the imposition of such high taxes on the great mass of the people entails of course a lowering of the stand-

ard of life and impairs the purchasing power of the large mass of the people, which is an important factor in national economic development.

This leads me to the most important question of all: Can the German economic structure bear this taxation burden in the long run? The year 1925 has afforded proof in Germany that taxes which are too high destroy economic prosperity. There sets in that vicious circle of business being depressed owing to high taxes, of the revenues of the States dropping on account of the depression and of the resulting deficit, which makes it necessary to resort to further tax increases.

For about a year our German economic structure has been upon a new basis, which we hope will prove sound and strong in the long run; for the time being no sufficient experience is available to foretell whether or not the sound basis will in the long run be disturbed and shaken by too high taxation, as many German industrialists contend. In particular, many in Germany entertain the fear that our ability to compete in world markets, on which our export trade depends, may come to be jeopardized by the pressure of German taxes.

My personal opinion is that, so far as we can survey the future, Germany will be able to make provision for the reparation burden under three conditions, of which the first depends on Germany alone, the second depends only in part on Germany, and the third is entirely dependent on world trade.

The first condition is that we in Germany work out our tax policy in such a manner as to eliminate all taxes which handicap production and constitute

a serious menace to our ability to compete in world markets.

I believe that the tax reform of the year 1926 has pointed out the path along which we ought to travel in the future; in the peculiar situation in which Germany finds herself in legislating upon taxation, fiscal and political considerations must never be allowed to gain the upper hand and economic considerations only are to be given first importance.

I spoke about the fundamental principles of this tax abatement in my third lecture and I pointed out that the Agent General in his report of November 30, 1926, said about this tax decrease: "The new taxation plan showed itself productive in an increasing measure." I am not going to enter upon details but I shall confine myself to a single example. The prohibitive taxation rates on consolidations and mergers of large companies had prevented a systematic consolidation of our metallurgical industry because, owing to the lack of capital under which German industry is laboring, it was all but impossible to raise the gigantic sums which had to be paid to the Treasury upon such transactions. The reduction and the occasional suspension of certain taxes opened the way to rationalization on a large scale, the success of which is now best illustrated by the German Steel Trust. There is no doubt that these reorganization measures contributed in an extraordinary degree to an improvement in the condition of German industry. So far as the Treasury is concerned, the tax abatement constitutes a most instructive example showing that the discarding of economically injurious taxes increases the revenue of the State instead of causing it to drop. The sum which

the German Steel Trust now pays to the German Federal Treasury every year, by way of income tax, amounts to many times the sum that the Federal Treasury might have collected by way of taxes on the merger before such taxes were repealed.

The Dawes Plan charges will in the long run make it necessary to resort to very high taxes in Germany but I have confidence (and the economic success of the tax reform of the year 1926 strengthens me in my belief) that by exercising the utmost economy in all public expenditures we may develop our tax system in such a way as to bring it about that our economic structure will be able to bear these taxes if the general commercial situation improves.

The second condition is that sufficient capital at reasonable interest rates be available to our economic structure to keep it on a high level of technical efficiency. A great deal of progress has been made through the rationalization measures of these last few years and I believe that further progress may be made along this line. At the same time we shall have to solve the question of standardization as it has been solved in America with such conspicuous success. In this connection, however, I must point out that the Germans are distinctly individualistic, a fact which is evidenced in politics by the circumstance that every German likes, if he can, to organize his own party.

But rationalization and standardization require very large capital investments. To mention only a few of the most important questions of the day, I shall refer to the development of our electrical power plants, the supply of long distance gas, the rebuilding of roads for automobile traffic, and the

construction of dwelling houses. All this requires a great deal of capital. It is a much-mooted question, so far as the formation of new capital is concerned, whether subtraction of a yearly sum of two thousand five hundred million gold marks will not so constrict our money market as to make sufficient financial reserves unavailable for industrial investment. In any case, Germany, if her industry is to keep pace with technical developments, will be compelled to borrow foreign capital for the technical improvement of her industrial equipment. Whether this can be done in the long run is something that only experience can teach us. In any case, this is a problem for the solution of which we must depend on foreign countries; in particular, on the U.S.A.

The third condition is that we succeed in utilizing our industrial equipment practically to its full extent. This will be possible only if to the internal consumption in Germany, which will rise slowly due to the lack of capital and to comparatively low salaries and wages, there is added an increasing export to foreign countries. It is clear that the matter depends to a large extent on the custom tariffs of the countries which import our goods, that is to say, it depends on whether Germany will be able to secure to German industry, through the conclusion of trade treaties, sufficient outlets abroad.

I believe you will agree with me that all these questions are of a very serious nature. The question as to Germany's ability to bear up under such taxation cannot at the present moment be answered definitely either in the affirmative or in the negative. My opinion is that we must reserve judgment until sufficient experience has been gathered in this new field.

However matters may develop in this connection, one thing can be stated definitely and without reservation: Germany will bend all her efforts to fulfill her obligations under the Dawes Plan and will effect punctually as she has heretofore the payments to be made to the Agent General. Nobody in the world has a right to doubt the good faith of Germany. This will entail great effort and the heavy tax burden made necessary by the Dawes Plan will undoubtedly create many political difficulties for the German Government, but we, upon whom has devolved the task of guiding New Germany, will tell our people again and again that our generation is to dispense with happiness and material welfare in order that we may bequeath to our children a Germany restored to freedom.

The heavy burden, however, on account of the imponderable psychological factors which control things in cases of this sort, can be borne only if performance is actuated, not by pressure from abroad, but by the free will of the people. Germany signed the London Ultimatum merely because she was compelled to do so under a threat of military action. She saw more machine guns and more tanks in German territory. The Dawes Plan was signed freely because we had confidence in the new spirit which is best embodied in the names of Charles G. Dawes and Owen D. Young. It is therefore a matter of national honor that we do everything in our power to meet these obligations. In earlier times those Germans who were in Hamburg and Bremen were described as "Honorable Merchants" and they made the German name honored and respected throughout the world. We want New Germany to restore to honor this fine

characteristic of Old Germany by bending her every effort to discharge loyally the commitments she has undertaken.

In my final lecture I shall picture with the utmost frankness the difficulties which in my opinion will arise in the carrying out of transfers under the Dawes Plan. Today I shall conclude my remarks by saying: I am fully aware of the burdensomeness of the charges that have been imposed upon the German people, but I am also fully aware of the determination of Germany to redeem her future by labor and by material sacrifices. The price, performance of our obligations under the Dawes Plan, is very high but for a great nation no price is too high, it seems to me, that is paid to uphold her honor and to secure her freedom.

LECTURE VI

THE PROBLEM OF TRANSFER AND OF GERMANY'S FUTURE

IN my fifth lecture I have given expression to the opinion that Germany, in spite of the great difficulties and dangers to which I am fully alive, will bend all her efforts to effect the Dawes Plan payments punctually. By these payments Germany's obligation under the Dawes Plan is fulfilled, as appears clearly and unequivocally in Section 12 of the Plan. This section reads:

All payments for the account of reparations will be paid in gold marks or their equivalent in German currency into the bank of issue to the credit of the agent for reparation payments. This payment is the definitive act of the German Government in meeting its financial obligations under the plan.

Here, however, the actual difficulties begin, which, unless a miracle occurs, are bound to increase year after year. I am now approaching the problem which constitutes the crucial point of the reparation plan, that is, the problem of transfers.

Throughout their unilateral dictation, up to the year 1923, the European Powers in their relations with Germany never seriously considered this question of transfer. They always started from the assumption that Germany, by means of oppressive taxation, was to squeeze out of her people for reparation purposes a few billion gold marks a year;

how these sums were to be transferred abroad without jeopardizing the German economic structure and German currency was never seriously considered by the victors. Apparently Germany was deemed to possess some magic power enabling her to convert paper money into English pounds sterling, or American dollars by means of some sort of philosopher's stone.

Dawes and his associates, with their insight into economic relationships, had a clear vision of the problem in all its ramifications. They felt that it was an entirely different matter to estimate the burden that Germany's economic and fiscal resources could bear from estimating the amount of her wealth that could safely be transferred abroad.

Dawes realized, furthermore, that the funds transferred to the Allies on reparation account could not, in the long run, exceed the sums which the balance of payments made it possible to transfer without currency and budget instability.

In Paragraph 8, of Section D, of the Dawes Report, we therefore meet with the following clear-cut statement:

For the stability of a country's currency to be permanently maintained not only must her budget be balanced, but her earnings from abroad must be equal to the payments she must make abroad, including not only payments for the goods she imports but the sums paid in reparations.

What is the state of Germany's balance of payments?

The most important factor in the balance of payments of every nation is the so-called balance of trade, that is to say, the ratio of exports to imports.

Germany has always shown, even in the years of her greatest wealth, a heavy surplus of imports over exports. Between the years 1900 and 1913 this comprised between one and two billion gold marks. The explanation of this fact is to be found in the circumstance that Germany must import large quantities of foodstuffs for the support of her population and that furthermore she is compelled to import from abroad most of the raw materials required for her industries, particularly the raw material for her textile industry. This necessity will always exist, for even under the pressure of reparation obligations cotton will not be prevailed upon to grow in Germany in order to facilitate transfers.

The adverse trade balance has increased considerably as a necessary consequence of the peace treaties. Germany has lost to Poland her agricultural districts in the east and the necessity for the import of foodstuffs has increased. She has lost to Poland in Upper Silesia a portion of her coal resources and practically all her tin and zinc resources. She has lost, in Lorraine, the control of her ores and she has also been deprived for fifteen years of her collieries in the Saar. Under such circumstances the surplus of imports over exports in the year 1924 amounted to 2.5 billions, in the year 1925 to 3.6 billions. The year 1926, which showed but a small import surplus, was quite abnormal; on the one hand there was the heavy German coal export brought about by the strike of the British miners and on the other the bountiful German crop of the year 1925 and, as the most important factor of all, the serious crisis of German industry which compelled all German manufacturers to curtail to the very minimum their im-

ports of raw materials. The year 1927 had already brought about a change in the situation; by June 20 the surplus of imports over exports had already attained a figure of 1.5 billion gold marks.

Prior to the War Germany's excess of imports was made possible by the balance of the so-called invisible exports and imports. Many indications point to the conclusion that the interest upon German capital invested abroad, the income of German shipping companies, and of German insurance companies (to mention only the most important items), amounted to more than the difference between the German imports and exports, so that Germany was becoming richer from year to year.

Even in this connection the situation has changed. German capital abroad has been confiscated except for the relatively small sums that were invested in the few neutral countries of Europe and in South America and the sums that have been released or are going to be released by former enemy countries such as South Africa and the United States of America.

We have been obliged to surrender our vessels and instead of transporting over the seas foreign goods under our flag, Germany had to transport her own goods under foreign flags. Germany has bent every effort to reconstitute a fleet of merchantmen of her own and she has done so, I believe, sooner than it was expected. However, at this very moment Germany has only a fraction of her 1913 tonnage.

In the case of the insurance companies, the situation is still more disheartening. In this field the collapse of the German currency has played havoc and the restoration of the formerly flourishing German insurance business will be an extremely difficult task.

With the tourist traffic I shall deal later on.

We are, then, confronted with the fact that Germany at the present moment has an adverse trade balance greater than before the War and that the invisible items give a balance which is a debit and not a credit, particularly if we take into account the loans raised abroad since the stabilization of the currency. We have no exact statistics on the entire indebtedness incurred by Germany since the conclusion of peace. S. Parker Gilbert estimates in his last report that at the end of 1926 the long-term indebtedness of Germany, including the Dawes Loan, amounted to one billion dollars. As this debt was contracted at comparatively high rates of interest, there is required for the interest and amortization service of this long-term indebtedness alone an annual sum of \$80,000,000 to \$100,000,000 which further impairs the German balance of payments.

These figures are sufficient to show the great difficulties standing in the way of the transfer of the reparation sums. The authors of the Dawes Plan fully realized these difficulties. In their plan they start from the assumption clearly set forth in Section 8, Paragraph D, in these words:

Reparation can only be paid abroad by means of an economic surplus in the country's activities.

Realizing the situation as to the German balance of payments and trade balance they state in Section 14:

In order that no difficulties with exchange or stability can possibly arise the sum payable for reparation may be definitely fixed at such a figure as is certain beyond all doubt to be within Germany's capacity to export in excess

of her imports. In this case the attainment of such certainty would involve so low a figure as to be quite unacceptable to her creditors and unwarrantably favorable to Germany.

This point is in my opinion the only point in the Dawes Plan where economic considerations are influenced by political. The experts saw clearly that the present situation of Germany offers the possibility of effecting the transfer out of an economic surplus of but a very small sum; at the same time they told themselves that the fixing of such a small sum would never be accepted by the Allied Powers so that the entire painstaking and meritorious labor of the Dawes Plan would be doomed to failure. So they assessed the reparation obligation at a higher figure than in their opinion was justified by the economic situation of Germany, in the hope that circumstances would better themselves in the future.

Is such a hope warranted?

To ask such a question is to start a survey of the chances of improvement of the German balance of payments. I take up first the exports and imports. Theoretically the transformation of the German surplus of imports into a surplus of exports is possible either through a decrease in the imports or an increase in the exports. If the German population is kept by low salaries and wages at a low standard of living, its impaired capacity to consume will of course become apparent in smaller import requirements for purposes of consumption; the German people will then import less wheat and less cotton (to give but a few examples) and this will improve the trade balance. But I fear that world trade would be seriously affected by such a weakening of the Ger-

man people as purchasers in the world market and I believe that many countries, in particular, the United States, would find such a solution very objectionable.

The second alternative is that, imports remaining constant,—exports be increased considerably. This in turn is dependent on two conditions: (1) that we in Germany produce better or cheaper than other countries; (2) that the countries of the world permit the importation of cheap German articles without burdening them with excessively high customs duties. The increase of German exports would have to be a very considerable one. Keynes shows in his last essay, "The Coming Crisis in Reparations," published in America in *The New Republic* on August 3, 1927, that the increase in German exports, allowing for the imports of raw materials embodied in the exports, must amount to 40 or 50 per cent. These are practically impossible figures which in my opinion might be made possible by means of a flood of German exports based on very low wages.

Would not the other countries of the world adopt measures against such dumping? Would not employers and employees in all countries demand and obtain protective duties against such a flooding of the world?

I believe that this is beyond question. The world would observe, were this experiment to be attempted in connection with reparations, the fulfillment in a new strange sense of the old saying from the Bible, "It is more blessed to give than to receive."

We may conclude that a German export surplus of any considerable amount is not to be expected and that, on the contrary, extraordinary efforts will have

to be made by Germany in order to avoid too great an import surplus. There remains for consideration only the question as to whether the so-called invisible factors may afford Germany a surplus for reparation purposes.

Here prospects are not so hopeless. I believe that we can obtain an increasingly greater surplus from the so-called "performance of services," in particular from the income of our ships, and I believe also that our insurance companies will gradually resume their growth.

The balance arising from the tourist traffic may become an important factor. Unlike the French, the Germans have always been a people fond of traveling and for more than a thousand years, since the time when the old German Emperors made their journeys to Rome, every German has entertained a longing to see the south. Our tourist balance has therefore always been an adverse one, but I believe that a change in this relation has occurred since the War. On the one hand the passion for travel on the part of the Germans has been checked by the impoverishment of the middle classes of society who used to travel most. Instead of a four weeks' trip to Switzerland or Italy, the German belonging to the middle classes now looks forward to one or two weeks' vacation in the mountains or in the German woods. On the other hand, due mainly to the comparatively low cost of living in Germany, the influx of foreign tourists has increased—with the exception of the Russians.

How extensively the tourists' traffic may influence the balance of payments is shown by the circumstance that according to a recent estimate by Dr.

Julius Klein, of the Department of Commerce, tourists from the United States alone spend \$650,000,000 a year in Europe, of which sum more than \$250,000,000 is spent in Paris. It appears to me within the bounds of possibility that a heavy influx of foreign tourists into Germany may facilitate the task of transfer. Every American who comes to Germany to visit a museum or to hear an opera may have the satisfaction of knowing that he has somewhat lightened the heavy responsibility resting upon the shoulders of S. Parker Gilbert.

But to speak seriously, all the invisible factors must undergo an increase which is hardly conceivable in order to make the transfer possible. As a matter of fact, the transfer in the latest years has been made possible only by the fact (and in the near future the situation will not be very different) that Germany has contracted loans abroad to take care of the deficit of her balance of payments. The interest and amortization service on these loans will make the problem of transfer increasingly difficult as the years go by. It is hardly conceivable that the transfer be handled throughout the whole period by having other countries, in particular America, lend money to Germany so that Germany may pay reparations.

Loans must be regarded as merely a temporary emergency device. This device was useful during the years in which relatively small sums were to be transferred; as soon as the annual payments reach two thousand five hundred million gold marks it will become necessary to decide what sum may be transferred out of the surpluses of German industry and trade without the help of new foreign loans.

It is clear that Charles G. Dawes and his associates, in their wisdom and farsightedness, fully realized this problem and the experts' report itself shows the path by which relief in these difficulties is to come.

In Paragraph 13 of the experts' report it is clearly stated:

If the payments by Germany on reparation account in the long run exceed the sums that can be thus transferred by deliveries or be purchased in foreign currencies, they will of course begin to accumulate in the bank. Up to a certain point, in normal circumstances not exceeding two milliards, these accumulations will form part of the short money operations of the bank.

Beyond this point, the Committee will find employment for such funds in bonds or loans Germany under the conditions laid down in the annex, but for economic and political reasons an unlimited accumulation in this form is not contemplated. We recommend that a limit of five milliards be placed upon all funds accumulating in the hands of the reparation creditors in Germany. If this limit is reached, the contributions from the budget are to be reduced below the standards set out in our plan, so that they are not in excess of the withdrawals from the account and the accumulation is not further increased. In this contingency the payments by Germany out of the budget and the transport tax would be reduced until such time as the transfers to the Allies can be increased and the accumulation be reduced below the limit named.

In these words the experts deal with the crucial matter and at the same time show the way out of a possible *impasse*. The Dawes Plan itself is so elastic and takes future contingencies into consideration to such an extent that, in order to avoid difficulties arising from the question of transfer, it is merely

necessary to apply the plan in the spirit of the authors of the report, that is to say, in a spirit of economic reasonableness. I believe that the agreement which I, as Minister of Finance, made with the Agent General, concerning Germany's so-called supplementary budget contribution, makes a valuable precedent. If difficulties arise, as, in my opinion, they must, in this matter of the transfer, a conference will be called around a green table and a way out of the difficulties will be sought and will be found.

There will be various ways out of the difficulties in any particular case. The important point is that the fundamental principle of the Dawes Plan must be upheld. Here the interest of the powers who are receiving reparations is the same as the interest of Germany. Reparations must never be allowed to bring about such a state of German economic life and of German currency as will affect the economic condition of the world at large and destroy the ability of the Germans to pay reparations.

Before the War frequent reference was made to the concert of Europe. Since the War this concert became somewhat discordant. The instruments are out of tune and no one is present to mark the tempo and bring the instruments into harmonious accord. The Dawes Plan affords the possibility of restoring harmony. It will be sufficient if all the *virtuosi* in the concert of the European Powers are willing to keep the tempo marked by the conductor. This tempo, if Europe's economic condition is to be reorganized and made sound, must be that spirit of economic thought and of fair play which is embodied in such men as Charles G. Dawes and S. Parker Gilbert.

No one may prophesy with certainty, but if I were

to assume for a moment the rôle of a prophet, I might summarize my personal opinions as to further developments under the Dawes Plan thus: Germany will meet her obligations punctually and the Agent General will be able in the near future, particularly if the release of German property in America is consummated, to transfer successfully a large portion of the German payments. Later on he will be compelled, as is contemplated in the Dawes Plan, to allow to accumulate in Germany the money originating from German payments which he cannot transfer. He will not desire to wait until the accumulated sum reaches five billions. The time will come, therefore, when a conference will be held to consider how, either by the issue of bonds created under the Dawes Plan and their offer on the world market or by other means, German reparation payments may be organized, according to the spirit of the experts' report, in such a manner as to avoid any great disturbance of the economic situation of the world.

When this time will come no one can tell. It will depend on the economic state of the world and on Germany's internal economic situation.

Germany, however (this I repeat is beyond doubt), will effect her payments loyally and punctually in spite of the political dangers to the German Government and to the German Republic, out of her heavy burden of taxation. History teaches us that people are prone to forget and that, as a rule, they see only the present, seldom the future, never the past. In Germany this leads to the following situation which has important political reverberations: The Monarchy lost the War—this is forgotten; the Republic has to carry out the Peace Treaty and to pay for the

War—this is felt every day. As the great mass of the people is influenced by present facts and does not bother about reasons, many groups in Germany blame the Republic for high taxes or for the loss of Upper Silesia or for the occupation of the Rhineland. During the last year this won the enemies of democracy many followers; but order was brought into our internal economic situation, the spirit of Versailles was thrust aside by the spirit of Locarno in the conduct of our foreign policy, and as a result the hopes of the radicals have sunk and, in my opinion, they will sink still further if no further disturbance arises on the economic or political horizon.

Viewing the situation today, it seems established beyond the slightest doubt that the democratic republic in Germany is completely consolidated. It is possible, although not likely in my opinion, that, were an unfavorable situation to arise, such as a setback in our policy of international conciliation or the outbreak of a new economic crisis, powerful efforts would be made to overthrow the republic. It is certain that such endeavors, as the Kapp *putsch* in the year 1920 and the Hitler *putsch* in the year 1923, will fail.

The great majority in Germany holds fast to the new Constitution. The very fact that such a man as the present President of the Reich, von Hindenburg, who is revered by all Germans, has sworn allegiance to the Constitution and staunchly maintains his loyalty, as was to be expected from a man of such a straight and strong character, has strengthened and consolidated the German Republic. War, revolution, collapse of the currency are things of the past. We are now building a new Germany.

If you come to see us you will no longer find, as in the era of Wilhelm II, courtly ostentation and military pomp, but you will find the Germany of Albrecht Dürer, of Ludwig van Beethoven, of Immanuel Kant and of Goethe, more clearly recognizable than in recent decades. The years of great wealth have not always been the best in German history. This is shown by the era after the 1870-1871 war when the billions paid by France to Germany were not a blessing but a curse for the German people. New wealth led them to the terrible period of the so-called creative era when in all the German cities there grew from the ground gigantic houses of very bad architecture. Behind their ugly and ostentatious façades, they concealed an uncultivated interior. Our entire political and cultural life presented the same aspect; many things were false and intended for external effect. Things were done for exhibition purposes. New Germany has no ostentatious façades, but I believe that inside the house many things present a better appearance; in our poverty we have retraced our steps from Potsdam to Weimar and in my opinion Weimar is better and more truly German than Potsdam.

We believe in our future and we are educating our youth for this future—not, as formerly, to be soldiers of the emperor, but to become a healthy generation that will know what it works for and will take its part in the large cultural activities of our nation and of the world.

This is the meaning of the new youth movement in Germany; we want a new German youth to grow up, bronzed by the air and steeled by sports, enjoying

the sun and the wind, the blossoms and the snow, the whole inspiring happiness of our country.

Such a generation will have a true comprehension of internal and external freedom as one of the greatest treasures of mankind and will be able to appreciate it at its full value. Our German policies at large will then be directed toward securing this liberty for our children.

To this end there is for Germany—in my firm conviction, which is shared by the very large majority of the German people—but one way: the way of labor. We know that, if we desire to tread this path with success, we must refrain from all adventurousness in foreign politics and we must always bear in mind that the strength of the vanquished is forbearance.

This is a task demanding self-denial, but I believe that it is, at the same time, a great and beautiful task. Everything depends on the spirit in which we carry out this task of the German people in the years to come. What appears on the surface to be unheroic may be done in a heroic spirit.

The path that lies before the German people is a painful one; the milestones along this path are poverty, forbearance, and hard work. But a new Germany will tread this path, and I believe that at the end of the struggle there will dawn for the German nation the day in which the long winter of our discontent will be made glorious summer by the sun of democracy and freedom.

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